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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938 ~~/~~ 9

No. ~~854~~ 30

THE UNITED STATES OF AMERICA, PETITIONER

vs.

THE GLENN L. MARTIN COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR CERTIORARI FILED APRIL 8, 1939

CERTIORARI GRANTED MAY 1, 1939

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 854

THE UNITED STATES OF AMERICA, PETITIONER

vs.

THE GLENN L. MARTIN COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

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1 [Caption omitted.]

2 IN DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF MARYLAND

At Law. No. 6239

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, PLAINTIFF

vs.

THE UNITED STATES OF AMERICA, DEFENDANT

Amended petition

Filed December 14, 1937

The petition of The Glenn L. Martin Company, plaintiff, respectively shows and alleges:

1. The plaintiff, The Glenn L. Martin Company, is a corporation duly organized and existing under and pursuant to the laws of the State of Maryland, with its principal place of business at Middle River, Baltimore County, Maryland.

2. This is an action for breach of a contract, entered into between plaintiff and defendant, by the defendant, the action being filed for the recovery of the sum of $7,737.32, exclusive of interest and costs, representing amounts paid by plaintiff applicable directly upon the production of certain supplies called for under the terms of the said contract, the defendant having refused, in violation of the terms of the said contract, to repay to plaintiff the said sum of $7,737.32 or any part thereof. This Court has jurisdiction of the controversy under Sub-division 20 of Section 41 of Title 28 of the United States Code, the amount involved, exclusive of interest and costs, being $7,737.32.

3. On or about June 28, 1934, plaintiff and defendant entered into a contract (U. S. Army Contract No. W535 ac-6861) under which plaintiff agreed to supply to defendant and defendant agreed to purchase and accept from plaintiff certain aircraft and aircraft materials. Article 17 of the said contract provided in part that:

"(3) It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any
3 Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies

herein contracted for then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

4. During the years 1936 and 1937 plaintiff made certain expenditures for labor in connection with the performance of the said contract, which expenditures were applicable directly upon the production of the supplies called for by the said contract. Of the said expenditures the sum of $769,219.30 represented wages subject to the taxes imposed upon the plaintiff by Titles VIII and IX of the Social Security Act (Act of August 14, 1935, c. 531, 49 Stat. 620, 42 U. S. C. c. 7 (Supp)).

5. Federal Social Security taxes were imposed upon plaintiff by the said Act of August 14, 1935, on the said wages paid in the amount of $769,219.30 as follows:

Year	Wages	Title IX	Title VIII	Total
1936	$766,962.82	$7,669.63		$7,669.63
1937	2,256.48	45.13	$22.56	67.69
Totals	769,219.30	7,714.76	22.56	7,737.32

6. The sum of $7,737.32 has been paid by the plaintiff as Federal and State of Maryland Unemployment Insurance taxes and as Federal Old Age Benefit taxes in accordance with all due requirements of law, and in the amounts set out in paragraph 5 hereof.

7. No portion of the said sum of $7,737.32, paid as aforesaid, has been or will be deducted by the plaintiff from any wages or compensation for services paid to or for the account of any employee of the plaintiff or any other person or persons performing services for it.

4 8. By communication dated October 14, 1937, addressed to Lieut. Col. William F. Volandt, Wright Field, Dayton, Ohio (the person authorized under the terms of said contract to receive such communications), a copy of which is annexed hereto, marked Exhibit A, and prayed to be made a part hereof, the plaintiff requested the defendant to advise it of the manner in which the defendant should be billed for the aforesaid Social Security taxes paid by the plaintiff in the performance of *of* the said contract.

9. By communication dated October 18, 1937, and addressed to the plaintiff, a copy of which is annexed hereto, marked Exhibit B. and prayed to be made a part hereof, the defendant advised plaintiff that the claim of the plaintiff if made would not receive favorable consideration.

10. By communication dated October 25, 1937, addressed to the plaintiff, a copy of which is annexed hereto, marked Exhibit C, and

prayed to be made a part hereof, the defendant reaffirmed the position taken by it in its communication dated October 18, 1937.

11. By communication dated November 10, 1937, addressed to "The Finance Officer, Wright Field, Dayton, Ohio," the person authorized under the terms of the said contract to make payments on behalf of the defendant in accordance therewith, a copy of which is annexed hereto, marked Exhibit D, and prayed to be made a part hereof, the plaintiff forwarded its invoice to the defendant and requested payment in the amount of $7,737.32, representing said Social Security taxes paid on expenditures for labor made during the years 1936 and 1937 in the performance of the above contract. Said invoice is annexed hereto, marked Exhibit E, and prayed to be made a part hereof.

12. By communication dated November 24, 1937, addressed to the plaintiff, a copy of which is annexed hereto, marked Exhibit F, and prayed to be made a part hereof, the defendant, by the person authorized under the terms of the said contract to make payments in accordance therewith, refused to pay the said claim for Social Security taxes paid during the years 1936 and 1937 on the said contract, and returned the said invoice for cancellation.

5 13. All of the steps taken by the plaintiff to secure the repayment of the said taxes of $7,737.32, paid as aforesaid, were taken in accordance with the terms and requirements of the said contract between the plaintiff and the defendant.

Wherefore the plaintiff demands judgment against the defendant in the sum of $7,737.32 with interest thereon as provided by law, for costs and for such other and further relief as may be proper.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Counsel for Plaintiff,

2500 Baltimore Trust Building, Baltimore, Maryland.

[*Duly sworn to by M. G. Shook; jurat omitted in printing.*]

In United States District Court

Defendant's plea to amended petition

Filed March 14, 1938

The defendant, United States of America, by Bernard J. Flynn, United States Attorney for the District of Maryland, for pleas to the amended petition filed herein, and each and every count thereof, says:

1. That it never promised as alleged.
2. That it was never indebted as alleged.

BERNARD J. FLYNN,
United States Attorney.

6 In United States District Court

Docket entry

March 14, 1938—Issues joined.

In United States District Court

Verdict

May 7, 1938. Verdict for the Defendant.

In United States District Court

Judgment

May 10, 1938. Judgment on verdict absolute in favor of the defendant for costs.

In District Court of the United States for the District of Maryland

At Law. No. 6239

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, PLAINTIFF

vs.

UNITED STATES OF AMERICA, DEFENDANT

Bill of exceptions

Filed June 14, 1938

Be it remembered, that at the trial of this cause in the March Term, 1938, of this Court, the Honorable W. Calvin Chestnut presiding, the following proceedings were had, to wit:

Stipulation as to certain facts

It was stipulated and agreed by and between counsel for the Plaintiff and the Defendant that on June 28, 1934, the Plaintiff and the Defendant entered into a contract (United States Army Contract No. W535-ac 6861—"Standard Form No. 32—approved by the President June 10, 1927"), under which contract the Plaintiff agreed to supply to the Defendant, and the Defendant agreed to purchase from the Plaintiff, certain aircraft and aircraft materials; that following the passage of the Federal Social Security Act and during the years 1936 and 1937, the Plaintiff made certain expenditures as

7 wages for labor in connection with the performance of the said contract, on which wages Federal Social Security taxes were imposed; that by virtue of the provisions of Arti-

cle 17 (3) of the said contract (which Article is set out in full on page 14 of this Record and made a part hereof by the Court below), the Plaintiff claimed that it was entitled to recover from the Defendant all amounts paid by it as Federal or State of Maryland Social Security taxes on expenditures for labor made by the Plaintiff in the performance of the said contract; that, in furtherance of such claim, the letters attached to the petition of the Plaintiff were written and the replies set out and similarly attached to said petition received and that all of such letters were correct copies of the original letters so written and received.

Thereupon, the Plaintiff introduced in evidence its copy of the contract between it and the Defendant, with leave to substitute a photostatic copy thereof at the conclusion of the hearing. The contract so introduced was marked "Plaintiff's Exhibit No. 1."

Thereupon, Morgan R. Schermerhorn, a witness of lawful age, after being first duly sworn, was examined and testified as follows:

That he is and has been employed by the Plaintiff since April 1931, and that he is and has been since January 1937, the Assistant Treasurer of the Plaintiff; that he now has and did have charge of the books of the Plaintiff during the period in which the said contract was being performed; that during the years 1936 and 1937, the Plaintiff paid wages of $766,962.82 and $2,256.48, respectively, for labor charged to the performance of the said contract; that Social Security taxes were imposed on the wages so paid and were paid by the Plaintiff as follows: $7,669.63 (1% of $766,962.82) for the year 1936, of which amount $6,902.67 was paid to the State of Maryland under its Unemployment Compensation Act, and $766.96 was paid to the Commissioner of Internal Revenue—Baltimore, Maryland, under the Title IX of the Federal Act, and $67.69 (3% of $2,256.48) for the year 1937, of which amount $40.62 was paid to the State of Maryland under its Unemployment Compensation Act, and $4.51 and $22.56, respectively, was paid to the Collector of Internal Revenue—Baltimore, Maryland, under Titles IX and VIII of the Federal Act.

8 That the Plaintiff, in determining the costs allocable to each contract in process of completion in its plant follows the following accounting procedure; namely, a record is maintained of all direct labor costs on each contract and such direct labor costs are charged monthly to such contract. All costs other than direct labor (which includes all mechanical labor in the factory, such as tool and engineering labor) are charged to overhead on a monthly basis and each contract bears its share of overhead charges on a percentage basis, that percentage being the quotient of the total overhead for the particular month divided by the total direct labor costs for such month. For example, if the total direct labor costs and the total overhead costs of one month for all contracts amounted to $100,000.00 and $50,000.00, respectively, the monthly overhead charges allocable to each contract would be 50% of the direct labor costs

charged to such contract. If four contracts were in process of completion at the same time, the direct labor and overhead costs of all contracts being $100,000.00 and $50,000.00, respectively, overhead costs would be allocated in the following manner:

Contract	Direct labor costs	Percentage	Overhead costs
A	$40,000.00	50%	$20,000.00
B	30,000.00	50%	15,000.00
C	20,000.00	50%	10,000.00
D	10,000.00	50%	5,000.00
Totals	100,000.00		50,000.00

That the above accounting practice was followed in determining the direct and overhead labor costs under the contract here involved, and that he, the said Morgan R. Schermerhorn, prepared a detailed break-down of the labor costs of $766,962.82 and $2,256.48, allocable to the said contract for the years 1936 and 1937, respectively, from the books of the Plaintiff; that such break-down, introduced in evidence as "Plaintiff's Exhibit No. 2," reveals the following in summarized form:

9 THE GLENN L. MARTIN COMPANY

Total labor charged to Army Contract No. W535 ac—6861 from January, 1936, to May, 1937, inclusive

Item No.		1936	1937
1	Direct labor	$544,679.95	$1,560.82
2	Tool labor	5,430.68	2.80
3	engineering labor	6,757.12	18.23
4	Overhead labor (direct and tool)	200,549.99	672.35
5	Overhead labor (engineering)	9,545.08	4.28
6	Total labor costs	766,962.82	2,256.48

That Item 4 (Overhead labor—direct and tool) was determined as follows: (a) the percentage of overhead allocable to each contract for the particular month was determined, as set forth above, by dividing the total direct labor costs (direct, tool, and engineering labor) into the total factory overhead costs (exclusive of engineering overhead) for such month; (b) the total labor costs included in such factory overhead were then determined; and (c) the percentage determined in (a) was applied against the total labor included in factory overhead for such month and the result was the direct and tool overhead labor allocable to the particular contract for such month. Item 4 represents the yearly total of the amounts so determined for each month.

That Item 5 (Overhead labor—engineering) was determined in the same manner by applying the percentage which the engineering over-

head applicable to the particular contract bore to the total engineering overhead for all contracts against all tool labor included in engineering overhead.

That all taxes, including Federal and State of Maryland Social Security taxes, paid by the plaintiff, except Federal and State income taxes, were included by the Plaintiff in overhead.

That the methods of accounting employed by the Plaintiff conformed to a standard code of accounting approved by the War Department of the Defendant; that a daily audit was made by the Defendant of the accounts of the Plaintiff during the performance of the said contract, and that a final audit thereof was similarly made when the contract was completed.

The above represents a summary of all the evidence in the case and, following oral argument by counsel, the Plaintiff moved for a judgment in its favor and then and there filed a motion in writing on the grounds therein stated, and the same was made a part of the Record, the said motion being as follows:

Motion for judgment

Comes now the plaintiff in the above entitled cause and moves the Court that judgment in said action be entered in favor of the plaintiff and against the defendant for the sum of seven thousand seven hundred thirty-seven dollars and thirty-two cents ($7,737.32) with interest thereon as provided by law.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.

The following prayers were submitted by the Plaintiff and the Court ruled on each of said prayers, in accordance with the views stated by it in its opinion, and noted exceptions for the Plaintiff as to adverse rulings:

Plaintiff's first prayer

The plaintiff prays the Court to rule as a matter of law that the evidence in this case is legally sufficient to entitle the plaintiff to recover and that, therefore, the verdict of the Court should be for the plaintiff. (Refused.)

Plaintiff's second prayer

The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract involved in this case were taxes applicable directly on the production, manufacture or sale of the supplies called for by the contract. (Refused.)

11 *Plaintiff's third prayer*

The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract in this case were taxes which were properly includable in plaintiff's cost of production of the supplies called for by the contract. (Refused—because, while academically correct, it is not of controlling importance in this case.)

Plaintiff's fourth prayer

The plaintiff prays the Court to rule as a matter of law that the requirements of the sentence appearing in Article 17 (3) of the contract between the plaintiff and defendant, namely:

"If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items" have been satisfied if such taxes were imposed by Congress after the contract was signed, were paid by the plaintiff and increased the cost of production of the supplies called for by the contract. (Refused—see Opinion.)

Plaintiff's fifth prayer

The plaintiff prays the Court to rule as a matter of law that if the sentence appearing in Article 17 (3) of the contract between the plaintiff and defendant—

"If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein con-
12 tracted for, then the prices herein stipulated will be increased or deceased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items" is interpreted literally, no sales tax or processing tax could be recovered because such taxes are not imposed on the articles sold or processed but are imposed upon the sale or processing of such articles. (Granted—But see Opinion.)

Plaintiff's sixth prayer

The plaintiff prays the Court to rule as a matter of law that the intent of the parties to the contract was to increase the stipulated

prices by an amount equal to new taxes or charges imposed by Congress after the contract was signed which increased the cost of production and to decease the stipulated prices by an amount equal to any decrease in the cost of production occasioned by changes in rates, made by Congress after the contract was signed, of taxes which were in effect when the contract was signed. (Refused—See Opinion.)

Plaintiff's seventh prayer

The plaintiff prays the Court to rule as a matter of law that whether social security taxes are, for accounting purposes, treated as items of cost or as items of overhead, the cost of production in either case should be increased by the amounts of such taxes paid with respect to labor engaged in the production of the supplies produced, manufactured, or sold. (Refused as academic—See Opinion.)

Plaintiff's eighth prayer

The plaintiff prays the Court to rule as a matter of law that the total amount of the social security taxes paid to the United States and to the State of Maryland during the year 1936 and 1937 with respect to wages paid to labor engaged in the performance of the contract, was imposed by Congress under Titles VIII and IX of the Federal Social Security Act. (It is unnecessary to rule on this proposition—See the Opinion.)

13 *Ruling on plaintiff's request for findings of fact and conclusions of law*

The Plaintiff filed a written request for findings of fact and conclusions of law, but the requested findings were refused by the Court, the reason for such refusal being noted on such request for findings in the following language:

"Request refused because facts found have been stated in the opinion in the case and conclusions of law requested are rejected as unsound or immaterial."

Following due consideration, the Court made an entered its opinion, directing the verdict to be entered in favor of the Defendant and denying the Plaintiff's motion for judgment in the following language:

"Motion overruled—see opinion in the case."

In such opinion, the Court allowed the Plaintiff timely and separate exceptions to the granting of the Defendant's motion for judgment, to the denial of the Plaintiff's motion for judgment, and to the refusal of the Plaintiff's first, second, third, fourth, sixth and seventh prayers, and to the refusal of the Court to grant or refuse the Plaintiff's eighth prayer. The judgment of the Court was entered on May 10th, 1938.

And now, in furtherance of justice and that right may be done, the Plaintiff tenders and presents the foregoing as the Bill of Exceptions

in the appeal from the action of the Court in the foregoing case, and prays that the same may be settled, allowed, signed, and sealed by the Court and made a part of the Record to be transmitted to the United States Circuit Court of Appeals for the Fourth Circuit.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.

Order settling bill of exceptions

The foregoing Bill of Exceptions duly allowed, settled, signed, and sealed, this 11th day of June, 1938.

W. CALVIN CHESNUT,
United States District Judge.

No objection as to form:
BERNARD J. FLYNN,
U. S. Attorney.
G. RANDOLPH AIKEN,
Asst. U. S. Attorney,
Attorneys for Defendant.

14 In District Court of the United States for the District of Maryland

At Law. No. 6239

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, PLAINTIFF

vs.

UNITED STATES OF AMERICA, DEFENDANT

Opinion

Filed May 7, 1938

CHESNUT, District Judge.

This is an action at law against the United States under the Tucker Act (28 U. S. C. A., s. 41 (20)). Such a suit is of course tried without a jury. The plaintiff, The Glenn L. Martin Company, a Maryland corporation with its principal place of business in Baltimore County, Maryland, is suing the Government to recover $7,737.32 (with interest) which is alleged to be due as extra compensation under its contract with the Government dated June 28, 1934, for the sale and delivery of certain aircraft and aircraft materials. In Article 17 (3) of the contract there was the following provision:

"(3) It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge and other taxes or charges are

imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein, and are paid by the contractor on the articles or supplies herein contracted for, then the price herein stipulated will be increased or decreased accordingly and any amount due the contractor as the result of such change will be charged to the Government and entered on vouchers as separate items."

The plaintiff claims the extra compensation under the second
15 sentence of this provision, by virtue of the incidence of taxes paid by it under the Act of Congress known as the Social Security Act of August 14, 1935, ch. 531, 49 Stat. 620; 42 U. S. C. A. (Supp. ch. 7). This Act was passed and became effective after the making of the contract. Under the Act and during the performance of the contract by the plaintiff, the latter paid in wages to employees allocated to work in the performance of the contract, $766,962.82 in the year 1936, and $2,256.58 in the year 1937. Under Title IX of the Act the plaintiff paid taxes (at the rate of 1%) on wages for the year 1936, $7,669.63 and for the year 1937, $45.13, and in the latter year also paid $22.56 taxes under Title VIII of the Act. The total taxes so paid by the plaintiff on wages of employees, during the performance of the contract, for the two years amounted to $7,737.32. Of the total amount so paid $7,714.76 was paid for unemployment insurance under Title IX of the Act, 10% thereof being paid to the federal government and 90% (if allowed by the Act of Congress) being paid to the State of Maryland under the Maryland Unemployment Compensation Law, Laws of Maryland, Extraordinary Session December 19, 1936, ch. 1. No part thereof will be deducted from wages due to employees, that is to say, the taxes are in addition to the wages paid.

In due course the plaintiff rendered bills to the Government for the amount of the taxes so paid, $7,737.32, but payment has been refused on the ground that it is not due under the wording of the contract. The question presented is whether by the effect of the Social Security Act the taxes so paid were "made applicable *directly* upon production, manufacture, or sale of the supplies called for herein and are paid by the contractor *on* the articles or supplies herein contracted for." [Italics supplied.] It will be noted that the plaintiff contractor must show that the taxes were (1) made applicable directly on production *and* (2) paid on the supplies.

The primary contention advanced by the Government is that the Social Security taxes were not at all imposed upon production, manufacture or sale, or *on the articles* or supplies contracted for because they are *excise taxes on the employer*, for the benefit of having employees, and were described by the Supreme Court in Steward Machine Co. v. Davis, 301 U. S. 548, 578, as follows:

16 "The tax which is described in the statute as an excise is laid with uniformity throughout the United States as a duty, an impost or an excise *upon the relation of employment.*" [Italics supplied.]

See also Helvering v. Davis, 301 U. S. 619. It is urged that the language contemplates a tax on or related to the production, or employment or use of physical property, while the Social Security Tax affects only the relation of employment, and is not associated in any way with tangible property. On the other hand the plaintiff contends that the fair and reasonable construction of the whole of the contract provision entitled it to recover the taxes so paid because they constituted "an increase in cost of production."

The contention of the Government sets up a construction of the wording which seems very narrow and literal. We must remember that we are construing a business contract rather than dealing primarily with a tax case. Batavia Mills, Inc., v. United States, Ct. Claims, June 1, 1937. And in a business or economic sense the taxes paid did result in an increase of the cost of production to the contractor. The general purpose of the clause doubtless was to indemnify the contractor against increased cost of production due to increased taxes imposed by subsequent Acts of Congress, although the scope of the indemnity must be limited by the language used. The construction should be reasonable in the light of the subject matter, rather than narrowly literal. In this view it does not seem of controlling importance whether the tax is classified as a tax or duty, an impost, or excise (Thomas v. United States, 192 U. S. 363, 370), or whether it is, in its purely legalistic concept, imposed on the employer upon the relation of employment, or on the product of the employment. A sales tax is an excise tax on sales rather than on the articles sold; and similarly a process tax is an excise on the act of processing rather than on the product. (See United States v. Butler, 297 U. S. 1, 57, 61.) It would seem fairly clear that such taxes would properly be regarded as within the language of the contract provision although not "paid by the contractor on the articles or supplies herein contracted for," unless excluded by other wording of the contract. See Willcuts v. Bunn, 282 U. S. 216, 228. By
like reasoning it would seem logical to hold that a tax on the
17. employer, measured by his payroll, which undoubtedly increases his production cost, might be regarded as a tax on production. It is, however, unnecessary to expressly so determine in this case, in view of the conclusion now to be stated with respect to the force of the word "directly."

The construction contended for by the plaintiff is too broad in that it ignores the significance of the word "directly" in the contract clause which provides for additional compensation only if the new tax is by the Act of Congress "made applicable directly upon production, manufacture, or sale of the supplies called for herein." The tax here dealt with is described in the taxing Act itself as an excise tax "with respect to having individuals in his employ." U. S. C. A., Title 42, s. 1101, s. 1004. And the Supreme Court has described it as "an excise upon the relation of employment." In other words, it is a tax on the employer measured by his payroll. It seems

quite clear that such a tax is not "applicable directly upon production, manufacture, or sale." It becomes payable irrespective of the product of the employment. In the economic sense it does increase the cost of production but its effect is indirect rather than direct. The nature of the tax is an enforced contribution by the employer for the ultimate benefit of employees generally, and it would seem to be similar in nature to other burdens placed upon an employer by law for the safety or welfare of employees, such as required fire escapes on high buildings, and sanitary regulations for working conditions. All such humanitarian requirements clearly do actually increase manufacturing costs although they operate indirectly through overhead expense rather than directly, as would increased wages paid for the work done. The wording of the contract provision taken as a whole is not susceptible of the broad construction contended for by the plaintiff and clearly is not equivalent to "any increased cost of production" caused by new taxation. New and additional state taxes, whatever their effect upon the cost of production, are clearly not included; and it is equally clear that the provision is not worded in such a way as to cover any and all additional Federal taxes because those that are included are definitely limited to such as are made applicable directly upon production, manufacture, or sale. It is, I think, impossible to escape the significance of the word "di-
18 rectly" in this context, as it is obviously an important word of limitation, of familiar legal use. See Liggett and Myers Co. v. United States, 299 U. S. 383, 386.

The plaintiff submits the argument that the function of the word "directly" in the contract clause is only to limit the generality of the words "other taxes or charges" and thus restrict their application to new taxes or charges "which increase the cost of production of the supplies called for;" thus for instance, excluding income taxes which do not increase the cost of production but simply diminish net profits, if any. But this seems an untenable construction of the phraseology because the new taxes comprehended in the context, whether specifically referred to as "sales taxes, processing taxes, adjustment charges" or in the general terms of "other taxes or charges" must all be "made applicable directly upon production, manufacture, or sale" in order to constitute the basis for additional compensation.

Counsel inform me that the contract provision here under consideration has appeared in many War Department contracts during a period of several years past, but that they have been unable to ascertain how the clause has heretofore been applied in actual practice, as a possible aid to construction. Reference has been made to the case of Batavia Mills, Inc. v. United States, decided June 1, 1937, by the Court of Claims. But that case is not in point here. The relevant provision in the contract there, after reference to "all sales taxes, duties, imposts, revenues, excise or other taxes applicable to the supplies" then in force was "if any new taxes are made applicable to such supplies by Congress after the date of opening of the

bid upon which this contract was based." then the price should be increased. The contractor with the Government in that case, in performance of its contract, had been obliged to pay an increased cost to its vendor by reason of processing taxes paid by the latter to the United States under the Agricultural Adjustment Act of May 12, 1933, as amended. The Court of Claims rendered judgment for the plaintiff contractor for the amount in dispute, but it will be noted from the opinion in the case that the Government's denial of liability was put "on the ground that said amount was not paid by the
19 plaintiff directly to the United States." And it will be noted that the contract provisions did not require as a condition for the additional compensation that the new taxes should be "made directly applicable to such supplies."

I conclude, therefore, that the verdict in this case must be for the defendant and the Clerk of the Court is instructed to so enter it to be followed in due course for judgment for the defendant with costs.

Both parties have requested the granting of certain submitted prayers on rulings of law, and I have ruled on them respectively in accordance with the view stated in this opinion and have filed them with the Clerk of the Court. Exceptions are noted for the plaintiff as to adverse rulings.

W. CALVIN CHESTNUT,
U. S. District Judge.

Dated May 7, 1938.

In United States District Court

Assignment of errors

Filed June 27, 1938

Comes now the Plaintiff, by its attorneys, Semmes, Bowen & Semmes and John T. Koehler, and makes and files the following Assignment of Errors upon which the Plaintiff will rely for the prosecution of its appeal from the judgment of this Court made and entered in the office of the Clerk of the District Court of the United States, for the District of Maryland, on May 10th, 1938:

1. The District Court erred in overruling the Plaintiff's motion for judgment for Seven thousand, seven hundred and thirty-seven dollars and thirty-two cents ($7,737.32), with interest.

2. The District Court erred in failing and refusing to enter judgment in favor of the Plaintiff.

3. The District Court erred in granting the Defendant's motion for judgment and in entering judgment in favor of the Defendant.

20 4. The District Court erred in refusing "Plaintiff's First Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the evidence in this case is legally sufficient to entitle the plaintiff to re-

cover and that, therefore, the verdict of the Court should be for the plaintiff."

5. The District Court erred in refusing "Plaintiff's Second Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract involved in this case were taxes applicable directly on the production, manufacture, or sale of the supplies called for by the contract."

6. The District Court erred in refusing "Plaintiff's Third Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract in this case were taxes which were properly includable in plaintiff's cost of production of the supplies called for by the contract."

7. The District Court erred in refusing "Plaintiff's Fourth Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the requirements of the sentence appearing in Article 17 (3) of the contract between the plaintiff and defendant, namely:

"'If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items' have been satisfied if such taxes were im-
91 posed by Congress after the contract was signed, were paid by the plaintiff and increased the cost of production of the supplies called for by the contract."

8. The District Court erred in refusing "Plaintiff's Sixth Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the intent of the parties to the contract was to increase the stipulated prices by an amount equal to new taxes or charges imposed by Congress after the contract was signed which increased the cost of production and to decrease the stipulated prices by an amount equal to any decrease in the cost of production occasioned by changes in rates, made by Congress after the contract was signed, of taxes which were in effect when the contract was signed."

9. The District Court erred in refusing "Plaintiff's Seventh Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that whether social security taxes are, for accounting purposes, treated as items of cost or as items of overhead, the cost of production in

either case should be increased by the amounts of such taxes paid with respect to labor engaged in the production of the supplies produced, manufactured, or sold."

10. The District Court erred in refusing to grant or refuse "Plaintiff's Eighth Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the total amount of the social security taxes paid to the United States and to the State of Maryland during the year 1936 and 1937 with respect to wages paid to labor engaged in the performance of the contract, was imposed by Congress under Titles VIII and IX of the Federal Social Security Act."

11. The District Court erred in concluding as a matter of law that no portion of the amounts paid by the Plaintiff as Federal and State Social Security taxes on labor engaged in the performance of the contract involved in this case was, within the meaning of Article 17 (3) of the contract, taxes applicable directly on the
22 production, manufacture, or sale of the supplies called for by such contract.

12. The District Court erred in concluding as a matter of law that the amounts paid by the Plaintiff as Federal and State Social Security taxes on direct labor engaged in the performance of the contract involved in this case were not, within the language of Article 17 (3) of such contract, taxes applicable directly on the production, manufacture, or sale of the supplies called for thereby.

13. The District Court erred in concluding as a matter of law that the amounts paid by the Plaintiff as Federal and State Social Security taxes on overhead labor engaged in the performance of the contract involved in this case were not, within the language of Article 17 (3) of such contract, taxes applicable directly on the production, manufacture, or sale of the supplies called for thereby.

Wherefore, the Plaintiff prays that the judgment of the District Court for the District of Maryland be reversed, and that the said District Court be directed to enter judgment for the Plaintiff in the amount of Seven thousand, seven hundred and thirty-seven dollars and Thirty-two cents ($7,737.32), with interest thereon, and for such other and further relief as to the Court may seem just.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.

In United States District Court

Stipulation as to exhibits attached to and forming a part of amended petition

Filed June 28, 1938

It is hereby stipulated and agreed, by and between the par-
23 ties to the above cause, in order to obviate the necessity for

including in the Record on Appeal the exhibits attached to and made a part of the amended Petition.

1. That the allegations of fact set out in Paragraphs 8, 9, 10, 11, and 12, with respect to the matters contained in Exhibits A, B, C, D, E, and F, are correct and set forth in substance the statements contained in such exhibits.

JOHN T. KOEHLER,
Attorney for Plaintiff.
BERNARD J. FLYNN,
United States Attorney,
Attorney for Defendant.

In United States District Court

Stipulation of counsel as to record on appeal

Filed June 28, 1938

It is stipulated and agreed by and between the parties to the above cause that the transcript of record for the appeal shall consist of the following:

1. Plaintiff's amended petition, omitting the attached exhibits,
2. Defendant's pleas to amended petition,
3. Stipulation as to exhibits attached to and forming a part of amended petition,
4. Docket entry of joinder of issue,
5. Verdict and judgment,
6. Bill of Exceptions,
7. Assignment of Errors,
8. Docket entries,
9. Stipulation as to record on appeal,
10. Opinion of Judge W. Calvin Chesnut,
11. Memorandum of the Clerk,
12. Order to transmit Record,
13. Clerk's Certificate.

JOHN T. KOEHLER,
Attorney for Plaintiff.
BERNARD J. FLYNN,
United States Attorney,
Attorney for Defendant.

In United States District Court

[Title omitted.]

Docket entries

1937

Decr. 14—Petition under Title 28, Sec. 41, Sub-division 20, U. S. Code, for breach of contract, filed. (Service admitted by U. S. Atty.)

Decr. 14—Affidavit of service of copy of petition on U. S. Atty. and of mailing copy to U. S. Attorney General, filed.

1938

Feby. 12—Petition of U. S. Attorney and Order of Court extending the time for filing pleas herein for thirty days from 12 February, 1938, filed.

Mch. 14—Pleas 1 & 2 filed. Issues joined.

Apr. 20—Case tried before Court (Chesnut, J.).

Apr. 20—Plaintiff's (8) and Defendant's (2) Prayers filed.

25 Apr. 20—Plaintiff's request for Findings of Fact and Conclusions of Law, filed.

Apr. 20—Pltff's motion for judgment filed.

May 7—Verdict for the Defendant, Opinion of Court, filed.

May 7—Judgment on Verdict nisi.

May 10—Judgment on Verdict absolute in favor of the Defendant for costs.

June 14—Plaintiff's Bill of Exceptions, filed.

June 27—Petition of Plaintiff for Allowance of appeal and Order of Court allowing appeal and fixing the penalty of the appeal bond in the sum of $300, filed.

June 27—Assignment of Errors, filed.

June 27—Citation issued retble within forty days. (Service acknowledged.)

June 28—Stipulation of Counsel re exclusion of Exhibits attached to amended Petition from record on appeal filed.

June 28—Stipulation as to Transcript of Record on Appeal filed.

In United States District Court

Memorandum of the clerk

(1) Petition for Appeal filed 27th June, 1938.

(2) Appeal granted 27th June, 1938.

(3) Appeal Bond dated 14th June, 1938. Obligors: The Glenn L. Martin Company, as principal, and Aetna Casualty & Surety Company of Hartford, Connecticut, as Surety. Penalty: $300.00, conditioned for costs.

(4) Citation dated 27th June, 1938. (Service acknowledged.)

26 In United States District Court

Order to transmit record

And, thereupon, it is Ordered by the Court here that a transcript of the record and proceedings of the cause aforesaid, together with all things thereunto relating, be transmitted to the said United

States Circuit Court of Appeals for the Fourth Circuit and the same is transmitted accordingly.

Test:

ARTHUR L. SPAMER,
Clerk, U. S. District Court.

[Clerk's certificate to foregoing transcript omitted in printing.]

27 In United States Circuit Court of Appeals for the Fourth Circuit

No. 4375

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

Appeal from the District Court of the United States for the District of Maryland, at Baltimore

Docket entries

July 16, 1938, the transcript of record is filed and the cause docketed.

Same day, the original petition for appeal, order allowing appeal, bond, and citation are certified up.

Same day, the appearance of John T. Koehler is entered for the appellant.

Same day, twenty-four copies of the printed record are filed.

July 28, 1938, the appearance of Jas. W. Morris, Assistant Attorney General; Sewall Key, Special Assistant to the Attorney
28 General, and Bernard J. Flynn, United States Attorney, is entered for the appellee.

September 17, 1938, stipulation as to the time for the filing of the respective briefs is filed.

29 *Addendum to transcript of record; printed at the instance of appellee*

Filed September 28, 1938

[Caption omitted.]

30 In United States District Court

[Title omitted.]

Supplemental stipulation respecting record

Filed September 16, 1938

Referring to the stipulations respecting the record on appeal which were heretofore filed on June 28, 1938, entitled, respectively, "Stipu-

lation as to Exhibits attached to and Forming a Part of Amended Petition" and "Stipulation of Counsel as to Record on Appeal," which appear at pages 22–24 of the printed transcript of record filed in the United States Circuit Court of Appeals for the Fourth Circuit in connection with the appeal heretofore allowed in this matter, at the request of the defendant, the plaintiff not agreeing that it is necessary to the determination of the issues involved in the appeal, it is now stipulated and agreed by and between the parties to the above cause that the papers attached to and made a part of the plaintiff's amended petition herein and described as Exhibits A, B, C, D, E, and F, respectively, which are referred to in Paragraphs 8, 9, 10, 11, and 12, respectively, of said amended petition, may be printed and transmitted to the Circuit Court of Appeals for the Fourth Circuit as an addendum to the record on appeal under Rule 14 of said Circuit Court of Appeals.

It is further stipulated and agreed that the Exhibit referred to in the Bill of Exceptions as "Plaintiff's Exhibit No. 1" (Transcript of Record on Appeals, page 7), may be transmitted to the Circuit Court of Appeals for the Fourth Circuit for consideration and inspection in connection with the appeal because it is impracticable to
31 have this Exhibit printed in the record or in any addendum thereto.

It is further stipulated and agreed that the Circuit Court of Appeals for the Fourth Circuit shall determine whether the appellant or appellee shall pay the cost of printing the addendum to the record and of forwarding to the said Court Plaintiff's Exhibit No. 1.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.
BERNARD J. FLYNN,
United States Attorney,
Attorney for Defendant.

32 In United States District Court

[Title omitted.]

Order for transmission of original exhibit to the United States Circuit Court of Appeals for the Fourth Circuit under par. 4, rule 14, of that court

Filed September 16, 1938

Whereas, it appears that it is necessary and proper that the original Exhibit, referred to in the Bill of Exceptions heretofore filed in this cause as "Plaintiff's Exhibit No. 1," be available for use and inspection by the United States Circuit Court of Appeals for the Fourth Circuit in connection with appellate proceedings herein; and

Whereas, it further appears that said Exhibit is of such a character that it would be impracticable to have it printed in the record or in an addendum thereto;

Now, therefore, the parties hereto, by their respective counsel, having agreed by stipulation heretofore filed to the transmission of the said original Exhibit to the United States Circuit Court of Appeals for the Fourth Circuit, as provided by Par. 4, Rule 14, of said Court, it is accordingly Ordered, by the District Court of the United States for the District of Maryland, this 16th day of September, 1938, that when the addendum to the record on appeal herein is forwarded by the Clerk of this Court to the United States Circuit Court of Appeals for the Fourth Circuit, that the said Clerk also forward said original Exhibit to the Clerk of the said United States Circuit Court of Appeals, to be kept by the said Clerk for use and inspection by the said United States Circuit Court of Appeals until the determination of the appeal, said Exhibit thereupon to be returned to this Court.

W. CALVIN CHESNUT,
United States District Judge.

33 *Exhibit A attached to amended petition of plaintiff*

OCTOBER 14, 1937.

From: The Glenn L. Martin Company, Baltimore, Maryland.
To: Lieut. Col. William F. Volandt, Wright Field, Dayton, Ohio.
Subject: Contract W 535ac-6861 dated June 28, 1934.
Reference: (a) Paragraph 3 of Article Seventeen of subject Contract.

1. In accordance with Paragraph 3 of Article 17, of the subject Contract, if any Sales Tax, Processing Tax, or other tax or charge is imposed by Congress subsequent to the date of the Contract, and made applicable directly upon the production, manufacture, or sale of the supplies called for in the Contract, and is paid by the Contractor, then the prices in the Contract are to be increased or decreased accordingly, and any amount due the Contractor as a result of such tax is to be charged to the Government as a separate item.

2. The Social Security Law, imposing an Unemployment Insurance Tax on all labor, was passed by Congress subsequent to the date of the subject Contract, and was operating as a tax to the extent of One Percent (1%) of the labor expended on the Contract in 1936. The Contract was completed in the Fall of 1936, and we are now preparing the necessary data for a separate invoice covering the amount of Social Security Tax which we paid on the labor used in prosecuting the Contract.

3. Will you please advise whether any special forms are to be filled out and submitted along with our invoice, and the proper procedure to follow in submitting this item for payment? We presume that the invoice is to be rendered, and will be approved for payment by your office in the usual manner.

Yours very truly,

THE GLENN L. MARTIN COMPANY,
By M. G. SHOOK, *Treasurer.*

34 *Exhibit B attached to amended petition of plaintiff*

In reply refer to EHA:bkh:63.

OCTOBER 18, 1937.

Contract W 535 ac-6861.
The GLENN L. MARTIN COMPANY,
Baltimore, Maryland.

1. Receipt is acknowledged of your letter of October 14, 1937, indicating your attention to file claim under paragraph (3) of Article 17 of subject contract for reimbursement of taxes at the rate of one percent (1%) of the wages paid by you for labor used in the manufacture of airplanes delivered to the Government under subject contract and in connection therewith requesting advice on appropriate procedure involved with particular reference to any special forms employed:

2. You state that the taxes for which reimbursement is to be claimed arise from the Social Security Law:

"Imposing an Unemployment Insurance Tax on all labor, which was passed by Congress subsequent to the date of the subject contract and was operating as a tax to the extent of one percent (1%) of the labor expended in the contract in 1936."

You further state that the subject contract was completed in the fall of 1936.

3. Subject contract provisions herein referred to stipulated:

"It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges
35 are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

Section 804, of the Act of August 14, 1935 (Social Security Act), provided, in pertinent part, that:

"In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 811) paid by him after December 31, 1936, with respect to employment (as defined in section 811) after such date:

"(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum."

4. Inasmuch as subject contract was completed, according to your statement, in the fall of 1936, it would appear that no taxes imposed

by the Act of August 14, 1935, should have been made with respect to employment involved in subject contract, but notwithstanding this fact it is obvious that there is no authority under the contract to make payment for the claim your have in mind. It will be noted that the tax which may be considered as an addition to the contract price is any sales tax, processing tax, adjustment charge, or other taxes imposed by or changed by the Congress subsequent to the date of the contract and made applicable directly upon production, manufacture, or sale of the supplies called for in the contract. The tax imposed by Section 804 of the Act of August 14, 1935, is not a tax upon the airplanes or parts delivered under the contract, but is a tax with respect to individuals in the employment of the contractor. It is a payroll tax and not a tax upon the production, manufacture, or sale of the airplanes.

36 5. This question has been previously considered by the Comptroller General of the United States and his opinion A-84124 dated March 6, 1937, is in accord with the information herein contained.

6. Accordingly you are advised that any invoice predicated upon the claim disclosed by your letter will not receive favorable consideration. It, therefore, appears unnecessary to advise you further with respect to proper procedure involved in an appropriate case.

For the Chief of the Material Division:

W. F. VOLANDT,
Lt. Colonel, Air Corps,
Chief, Procurement Section.

37 *Exhibit C attached to amended petition of plaintiff*

In reply refer to EHS: bkh: 63.

OCTOBER 25, 1937.

Contract W 535 ac-650

The GLENN L. MARTIN COMPANY,
Baltimore, Maryland.

1. Your letter dated October 21, 1937, file 3227, in further reference to the matter raised in your letter of October 14, 1937, file 3212, to which answer was made in letter of this office addressed to you under date of October 18, 1937, has been received.

2. It is noted that you invite attention to the fact that the claim you have in mind is to be predicated upon Section 901, Title IX, of the Act of Congress approved August 14, 1935, Public No. 271, 74th Congress, in lieu of Section 804 thereof as previously supposed by this office. So much of Section 901 considered by you as applicable to your claim is as follows:

"On and after January 1, 1936, every employer (as defined in Section 907) shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages (as defined in Section 907) payable

by him (regardless of the time of payment) with respect to employment (as defined in Section 907) during such calendar year:

"(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum; * * *"

Contract concluded in the fall of 1936.

3. It appears that Section 901 does have application with respect to individuals in your employment engaged upon subject contract in the year 1936, yet in the opinion of the Comptroller General
38 of the United States, A–84124, dated March 6, 1937, the tax imposed is not made applicable directly upon production, manufacture, or sale of the supplies called for under the terms of subject contract within the meaning of paragraph (3) of Article 17 thereof. It is, on the contrary, as heretofore advised, a pay-roll tax with respect to individuals in your employment at the time in question. Sections 804 and 901 are distinguishable only in the categories of employees to which they relate.

4. The information and advise heretofore conveyed to you in letter dated October 18, 1937, hereinabove referred to, is considered applicable to taxes imposed by Section 901 as well as Section 804 of the Social Security Act. A copy of the opinion of the Comptroller General of the United States, A–84124, is furnished herewith for your information and guidance.

For the Chief of the Material Division:

W. F. VOLANDT,
Lt. Colonel, Air Corps,
Chief, Procurement Section.

1 Incl.
Opinion of Comp. Gen. of U. S. No. A–84124 dated 3/6/37.

39 *Exhibit D attached to amended petition of plaintiff*

NOVEMBER 10, 1937.

From: The Glenn L. Martin Company, Baltimore, Maryland.
To: Finance Officer, Wright Field, Dayton, Ohio.
Thru: Representative, Air Corps, U. S. Army, Baltimore, Maryland
Subject: Claim for Refund of Social Security Tax—Forwarding o Invoice.
Reference: (a) Contract W 535ac-6861 dated June 28, 1934.
Enclosure: (A) 4 Copies GLM Invoice No. G-4108.

1. We are attaching hereto our Invoice No. G-4108 for $7,737.3 Enclosure (A), covering our claim for refund of Social Securit Taxes paid on total expenditures for labor during the years 1936 an 1937, on U. S. Army Contract No. W 535ac-6861, which was signe on June 28, 1934, which is prior to the effective date, i. e., August 1 1935, of the Social Security Act.

2. If the enclosed Invoice is not paid within thirty days, we wi assume that our claim is rejected; whereupon we will proceed to te the opinion of the Comptroller General of the United States N

A-84124 dated March 6, 1937, as we consider the Social Security Taxes applicable directly upon production, manufacture or sale of the supplies called for in the Contract, Reference (a), recoverable in full, as stipulated in Article 17, Paragraph 3, of the Contract.

Yours very truly,

THE GLENN L. MARTIN COMPANY,
By M. G. SHOOK, *Treasurer.*

MGS:P
c. c. W. Randall Compton of Semmes, Bowen & Semmes.

40 *Exhibit E attached to amended petition of plaintiff*

G-4108.

NOVEMBER 10, 1937.

W 535ac-6861 dated June 28, 1934. Net Cash.
FINANCE OFFICER, *Wright Field, Dayton, Ohio.*

Social Security Taxes paid on expenditures for Labor during the years 1936 and 1937, on U. S. Army Contract W 535-ac6861, signed on June 28, 1934, $7,737.32.

Total Claim in accordance with the following:

Year	Labor	Unemployment insurance tax	Old age benefit tax	Total claim
1936	$766,962.82	$7,669.63		$7,669.63
1937	2,256.48	45.13	$22.56	67.69
Totals	769,219.30	7,714.76	22.56	7,737.32

It is hereby certified that the above is correct and just, and that payment therefor has not been received.

THE GLENN L. MARTIN COMPANY,
By M. G. SHOOK, *Treasurer.*

41 *Exhibit F attached to amended petition of plaintiff*

HEADQUARTERS, WRIGHT FIELD,
OFFICE OF THE FINANCE OFFICER,
Dayton, Ohio, November 24, 1937.

Subject:
Social Security Taxes
Contract W 535 ac 6861
To: The Glenn L. Martin Company, Baltimore, Maryland.

1. Answering your letter of November 10, 1937 (MGS*P) to which you have attached Invoice G-4108 dated November 10, 1937, in amount of $7,737.32, covering claim for social security taxes paid during the years 1936 and 1937 on Contract W 535 ac 6861, be advised that this office is unable to pay this claim in view of Decision of the Comptroller General of the United States No. A-84124 dated March 6, 1937.

2. In view of the above, your invoice is returned for cancellation.

JOHN F. CONNELL,
Captain, F. D., Finance Officer.

42 [Clerk's Certificate to foregoing transcript omitted in printing.]

43 Same day, to wit, September 28, 1938, Plaintiff's Exhibit No. 1 is certified up.

In United States Circuit Court of Appeals

Minute entry of argument and submission

November 10, 1938, cause came on to be heard before Parker and Northcott, Circuit Judges, and H. H. Watkins, District Judge, and is argued by counsel and submitted.

44 In United States Circuit Court of Appeals, Fourth Circuit

No. 4375

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

Appeal from the District Court of the United States for the District of Maryland, at Baltimore

(Argued November 10, 1938. Decided January 9, 1939)

Before PARKER and NORTHCOTT, Circuit Judges, and H. H. WATKINS, District Judge.

John T. Koehler (Semmes, Bowen & Semmes on brief) for Apellant, and James E. Murphy, Special Assistant to the Attorney General (James W. Morris, Assistant Attorney General; Sewall Key, Special Assistant to the Attorney General; Bernard J. Flynn, U. S. Attorney, and G. Randolph Aiken, Assistant U. S. Attorney, on brief) for Appellee.

Opinion

Filed January 9, 1939

PARKER, Circuit Judge:

This is an appeal by plaintiff from an adverse judgment in
45 a suit instituted under the Tucker Act to recover of the United States the sum of $7,737.32, alleged to be due under a government contract because of plaintiff's being required to pay social security taxes in that amount. Under the contract, which was executed June 25, 1934, prior to the passage of the Federal Social Security

Act of August 14, 1935, 49 Stat. 620, plaintiff agreed, for a stipulated price, to supply to the United States certain aircraft and aircraft materials. That contract contained the following provision:

"It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any federal tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture or sale of the supplies called for herein and are paid by the contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

Something over a year after the execution of this contract Congress enacted the Federal Social Security Act, 49 Stat. 620, the following provisions of which are pertinent here:

"SEC. 804. In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages * * * paid by him after December 31, 1936, with respect to employment * * * after such date:

"(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum."

"SEC. 901. On and after January 1, 1936, every employer 46 * * * shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages * * * payable by him (regardless of the time of payment) with respect to employment * * * during such calendar year:

"(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum:

"(2) With respect to employment during the calendar year 1937 the rate shall be 2 per centum.

"SEC. 902. The taxpayer may credit against the tax imposed by section 901 the amount of contributions, with respect to employment during the taxable year, paid by him (before the date of filing his return for the taxable year) into an unemployment fund under a state law. The total credit allowed to a taxpayer under this section for all contributions paid into unemployment funds with respect to employment during such taxable year shall not exceed 90 per centum of the tax against which it is credited, and credit shall be allowed only for contributions made under the laws of states certified for the taxable year as provided in section 903."

Following the passage of the Social Security Act, plaintiff paid social security taxes in the amount of $7,737.32 for the years 1936 and 1937

on expenditures for labor employed in producing the supplies called for by the contract. Of this amount, $5,616.06 was paid as tax on sums paid to laborers engaged solely in the production or manufacture of these supplies. The remainder represents the portion of the tax paid on disbursements on account of "overhead" labor, and allocable to this contract, i. e., disbursements to employees who were engaged in production under other contracts as well as under the one here involved; and there is no contention that this allocation was not properly made in accordance with correct accounting principles. Of the total amount of the taxes paid, $6,943.29 was paid to the State of Maryland and credit on the federal tax was allowed therefor under section 902 of the Act quoted above.

47 The court below found for the government on the ground that the taxes paid by plaintiff were not "applicable *directly* upon production, manufacture, or sale" (23 F. Supp. 262, 264); and the plaintiff, having preserved its right of review by the presentation of appropriate prayers and exceptions duly entered, brings this appeal, contending that it is entitled, on the undisputed facts, to recover the amount sued for as a matter of law. The government contends that the judgment denying recovery should be affirmed, and that, in any event, plaintiff is entitled to recover no more than the amount of the taxes actually paid to the federal government, not including the part of the levies paid to the State of Maryland. Two questions, therefore, are presented for our consideration in interpretation of the contract sued on: (1) Whether the social security taxes imposed by the Act are "taxes or charges" made directly applicable upon production or manufacture; and (2) if so, whether that portion of the taxes paid to the State of Maryland and credited on the amount due under the federal Act are taxes "imposed by Congress" and "paid by the contractor" within the meaning of the contract. We think that both of these questions must be answered in the affirmative.

The taxes imposed by the Social Security Act are excise taxes and are so termed by the Act itself. They are imposed upon the relation of employment as one of the relationships embraced in the carrying on of business; and are sustained on the principle that "the power to tax the activities and relations that constitute a calling considered as a unit is the power to tax any of them. The whole includes the parts." Steward Machine Co. v. Davis, 301 U. S. 548, 581. Helvering v. Davis, 301 U. S. 619, 645. And because the tax is one upon the relation of employment, it is argued that it cannot be a tax "applicable directly" upon production or manufacture. We think, however, that, not this conclusion, but the contrary, is

48 the one which logically follows. As the whole is the sum of all its parts, a tax applicable directly on one of the parts is necessarily applicable directly on the whole which comprises it. The manufacture or production of the supplies called for by the contract necessarily involves the employment of labor and the use of mate-

rials; and a tax applicable directly upon either is a tax applicable directly upon the manufacture or production itself. No tax more directly applicable upon manufacture or production can be conceived, we think, than a pay-roll tax measured by wages paid to labor engaged therein.

It is argued that the contract should be interpreted as contemplating only taxes imposed by Congress on the production or manufacture of the particular articles called for by the contract and "measured by the number of units produced or sold or by weight or by some other unit of use or manufacture." We see no reason, however, to thus restrict the language used, which contains no provision that the tax imposed must be measured in any such way, but is of the broadest possible scope, including "any sales tax, processing tax, adjustment charge, or *other taxes or charges*." [Italics supplied.] The only limitation is that such taxes or charges be "applicable directly" upon production, manufacture, or sale; and, as we have seen, a tax "applicable directly" upon the employment of labor engaged in manufacture is "applicable directly" upon the manufacture or production in which that labor is engaged.

The language of the contractural provision is so clear, we think, as not to justify our looking beyond its plain meaning. If, however, we look to the purpose and intent of the parties, the provision was evidently inserted to protect the contractor against loss arising from the imposition of new or additional federal taxes, which would increase his cost of production but could not be anticipated with any degree of accuracy; and no tax could more clearly fall within the class of taxes which it was the purpose to provide against than
19 an employment tax measured by the wages paid to produce the articles which the contract called for. The taxes, it will be noted, are to be applicable directly upon the "manufacture, production, or sale" of the articles, not directly upon the articles themselves; and this requirement of directness is satisfied where the tax is imposed on some essential element of "manufacture, production, or sale" in such way as to constitute a direct burden upon same. It excludes, of course, such taxes as do not directly burden "manufacture, production, or sale," such as income, excess-profits, and capital-stock taxes.

The learned judge below was of opinion that the tax operated "indirectly through overhead expense rather than directly, as would increased wages paid for the work done." But a pay-roll tax measured by the wages paid to produce an article burdens production and increases the cost thereof to the same extent and in substantially the same way as increased wages. If the employer must pay three cents tax on every dollar paid in wages for the production of an article, the expense of producing the particular article is increased by just that much; and upon no possible theory can it be said that the tax is an investment of a permanent nature which would justify its being charged to overhead. And the settled accounting practice is that

such taxes should be charged to current expense and not to overhea
Cole, "Accounts; Their Construction and Interpretation," pp. 1
226, 227; Neuner, "Cost Accounting," p. 196; N. A. C. A. Bulleti
vol. XVIII, No. 24, Aug. 15, 1937, pp. 1376–1377.

Coming to the second question, i. e., whether the portion of t
tax paid to the State of Maryland and credited against the tax d
under the Act to the federal government falls within the meani
of the clause of the contract under consideration, it is to be not
that this portion, as well as the remainder, falls squarely within t
language used. The entire amount of the tax was "impose
50 by Congress and was "paid by the contractor." That a p
of it was paid with the consent of Congress to the State
Maryland and credited against the amount which would otherw
have been due under the Act, would seem to be immaterial. A ve
similar question was before the Court of Claims in *Batavia Mi
Inc.* v. *United States* (decided June 1, 1937, but unreported). The
a processing tax on cotton yarn had been paid by the manufactu
of cotton cloth to the seller of the yarn pursuant to the terms o
contract under which the yarn was purchased. The manufacturer
the cloth had sold it to the government under a contract providi
that the price should be increased by the amount of any new ta
made applicable by Congress to the supplies to be furnished after
date of the bid. In holding that the amount of the tax so p
might be recovered by the manufacturer of the cloth, who had
paid it to the government but to the processor of the yarn, the co
said:

"This is not a suit for the refund of taxes paid but an act
based upon the provisions of a contract. The provisions of the
with reference to refunds of taxes collected under the Agricultu
Adjustment Act have therefore no application. All of the matt
necessary to establish plaintiff's claim under the contract are sho
After the contract was entered into a new and additional tax
imposed on the manufacturer from whom the contract supplies w
purchased by plaintiff. The tax was passed on by the manufactu
and under the terms of plaintiff's contract with the manufactu
it was obliged to pay it. Defendant expressly agreed that the amo
of the tax should be added to the purchase price. The right
plaintiff to recover the amount so paid is clear and judgment
be rendered accordingly."

The Federal Social Security taxes were imposed by Congress
part of a comprehensive plan in which the states were expected
participate. That the states might be induced to do this, it was
vided in the Act that the taxpayer might credit against the
imposed by it any contributions paid by him into a state un
51 ployment fund, to an amount not exceeding 90% of the amo
of the tax under the federal Act. This, of course, was
more than permission to the taxpayer to pay to the state 90%
the tax imposed by the Act and to credit same as a deduction

the federal tax; and where the plaintiff availed itself of this privilege, paying a portion of the tax imposed to the state and claiming credit therefor under the Act, we think that it comes within the protection of the spirit as well as the language of the clause in the contract here under consideration. Even though the taxpayer was under legal obligation to pay the state tax to the state, the fact remains that that tax was imposed in connection with the general system brought into being by the federal Act and payment thereof was recognized as satisfying 90% of the obligation imposed by the federal tax. See Sections 903 and 904; Steward Mach. Co. v. Davis, 301 U. S. 548. If the state had not imposed a tax and established an unemployment fund complying with the requirements of the federal Act, the entire amount of the federal tax, without credit, would have been collected by the federal government and plaintiff would unquestionably have been entitled to recover same under the contract provision. We think it is in no worse plight because the state has seen fit to comply with the provisions of the federal Act and thus receive 90% of the tax that it imposes. The clause of the contract was intended to protect plaintiff against new taxes to be imposed by the federal government. It should not be denied this protection because that government permits a portion of the taxes imposed to be paid to the states under a general scheme for state and federal cooperation.

For the reason stated, the judgment appealed from will be reversed.

Reserved.

32 In United States Circuit Court of Appeals, Fourth Circuit

No. 4375

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

Appeal from the District Court of the United States for the District of Maryland

Judgment

Filed and Entered January 9, 1939

This cause came on to be heard on the transcript of the record from the District Court of the United States for the District of Maryland, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court appealed from, in this cause, be, and the same is hereby, reversed; and that this cause be, and the same is hereby, remanded to the District Court of the United States for the District of Maryland, at Balti-

53 more, with directions to set aside the verdict and grant a new trial in accordance with the opinion of the Court filed herein.

January 9th, 1939.

JOHN J. PARKER,
Senior Circuit Judge.

Recital as to issuance of mandate

On another day, to wit, February 9, 1939, the mandate of this Court in this cause is issued and transmitted to the District Court of the United States for the District of Maryland, at Baltimore, in due form.

Same day, the original petition for appeal, order allowing appeal, and bond are returned to the Clerk of the District Court at Baltimore, Maryland.

Same day, the original exhibit (Plaintiff's Exhibit No. 1) is returned to the Clerk of the District Court at Baltimore, Maryland.

54 [Clerk's certificate to foregoing transcript omitted in printing.]

55 Supreme Court of the United States

Order allowing certiorari

Filed May 1, 1939

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] Enter: Attorney General. File No. 43339. U. S. Circuit Court of Appeals, Fourth Circuit. Term No. 854. The United States of America, petitioner, vs. The Glenn L. Martin Company. Petition for writ of certiorari and exhibit thereto. Filed April 8, 1939. Term No. 854 O. T. 1938.

U. S. GOVERNMENT PRINTING OFFICE 1939

FILE COPY

SUPREME COURT, U.S.
FILED
APR 8 1939
CHARLES ELMORE CROPLEY
CLERK

No. [redacted] 30

In the Supreme Court of the United States

OCTOBER TERM, 1938

UNITED STATES OF AMERICA, PETITIONER

v.

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

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In the Supreme Court of the United States

OCTOBER TERM, 1938

No.—

UNITED STATES OF AMERICA, PETITIONER

v.

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

The Solicitor General, on behalf of the United States of America, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Fourth Circuit entered in the above cause on January 9, 1939, reversing the judgment of the District Court of the United States for the District of Maryland.

OPINIONS BELOW

The opinion of the District Court (R. 14–19) is reported in 23 F. Supp. 262. The opinion of the Circuit Court of Appeals (R. 43–48) is reported in 100 F. (2d) 793.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 9, 1939 (R. 48). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether taxes imposed upon respondent by Titles VIII and IX of the Social Security Act are taxes "applicable directly upon production, manufacture or sale" within the meaning of a contract by which the amount of such taxes imposed subsequent to the date of the contract are to be added to the stipulated price.

2. If the answer to Question 1 is in the affirmative, whether taxes levied and collected by the State of Maryland under its Unemployment Compensation Act for which a credit is allowed against the tax imposed by Title IX of the Federal Social Security Act are taxes "imposed by the Congress" within the meaning of such a contract.

STATUTES INVOLVED

The statutes involved will be found in Appendix A, *infra*, pp. 10–13.

STATEMENT

Respondent, a Maryland corporation engaged in manufacturing aircraft and aircraft material, brought this action in the District Court for the District of Maryland to recover $7,737.32 alleged to be due on a

contract with the War Department. The facts as found by the District Court (R. 14–19) are undisputed. They may be summarized as follows:

On June 28, 1934, respondent and the War Department entered into a contract under which that Company was to manufacture certain aircraft and aircraft materials for the Government at stipulated prices (R. 2, 14). The pertinent provision of the contract (Art. 17 (3)) reads as follows (R. 14):

> It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture or sale of the supplies called for herein, and are paid by the contractor on the articles or supplies herein contracted for, then the price herein stipulated will be increased or decreased accordingly and any amount due the contractor as the result of such change will be charged to the Government and entered on vouchers as separate items.

On August 14, 1935, Congress enacted the Social Security Act (c. 531, 49 Stat. 620). Thereafter, in 1936, respondent paid $766,962.82 and in 1937 paid $2,256.58 in wages to individuals in its employ who were engaged in the performance of this contract

(R. 15). The total wages paid for both years is $769,219.40.

Based on the wages so paid, the Martin Company for 1936 paid $766.96 to the Federal Government under Title IX of the Federal Social Security Act, and $6,902.67 to Maryland under that state's Unemployment Compensation Act.[1] These payments totaled $7,669.63. Under the same laws, the Company for 1937 paid $27.07 to the Federal Government ($4.51 under Title IX, and $22.56 under Title VIII), and $40.62 to Maryland, total payments of $67.69 (R. 7, 15). The total paid to both governments for these years is $7,737.32. Of this total, the amount paid to the Federal Government is $794.03 and the amount paid to Maryland is $6,943.29.

Demand for reimbursement based on Article 17 (3) of the contract, *supra*, for the total $7,737.32 paid to both Federal and State governments was refused (Addendum to Record, 5–13), and this suit was begun in the District Court to recover the full amount. That Court decided that the Federal Social Security taxes were not "applicable *directly* upon production, manufacture, or sale" (23 F. Supp. 262, 264), and gave judgment for the United States. It was therefore not necessary for it to decide the question whether the amounts paid to the State of Maryland were taxes "imposed by the Congress." The Circuit Court of Appeals decided both questions against the United States and reversed the judgment

[1] Laws of Maryland, Extraordinary Session, December 19, 1936, c. 1.

of the District Court (R. 48). Since there is no dispute respecting the facts, the decision of the Circuit Court of Appeals represents a judgment for respondent for the full amount paid to both Federal and State governments.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that taxes imposed by the Federal Social Security Act are "applicable directly upon production, manufacture or sale" within the meaning of the contract.

2. In failing and refusing to hold that the taxes imposed by the Federal Social Security Act are not "applicable directly upon production, manufacture or sale" within the meaning of the contract.

3. In holding that the taxes levied and collected by the State of Maryland under its Unemployment Compensation Act are taxes "imposed by the Congress" within the meaning of the contract.

4. In failing and refusing to hold that taxes imposed and collected by the State of Maryland under its Unemployment Compensation Act are not taxes "imposed by the Congress" within the meaning of the contract.

5. In reversing the judgment of the District Court.

REASONS FOR GRANTING THE WRIT

The court below holds that taxes imposed on respondent by Titles VIII and IX of the Social Security Act "with respect to having individuals in [its] employ" (Secs. 804, 901, *infra*, pp. 10, 11) are within

the meaning of Article 17 (3) of the contract by which the United States agrees to increase the prices stipulated therein by the amount of any subsequent taxes "imposed by the Congress" which are "applicable directly upon production, manufacture or sale" (R. 14). The court below also holds that taxes imposed, levied and collected by the State of Maryland under its Unemployment Compensation Act, for which a credit is allowed against the taxes imposed by Title IX of the Social Security Act are taxes "imposed by the Congress" within the meaning of Article 17 (3) of the contract. The decision on these questions, we submit, is erroneous, and is of large importance in view of the number of other contracts which contain the same or similar provisions.

A. The court below, in deciding that the taxes here involved are "applicable directly" upon manufacture or production, cited the language of this Court in *Steward Machine Co.* v. *Davis*, 301 U. S. 548, 581 that "The power to tax the activities and relations that constitute a calling considered as a unit is the power to tax any of them. The whole includes the parts." From that statement it drew the conclusion that those taxes are applicable upon manufacture or production, since employment is a necessary part of both (R. 45).

That result, as the District Court had pointed out (R. 17), fails to give any weight whatever to the word "directly." Taxes which might affect production or manufacture cannot be said to be "applicable directly" thereto, simply because of that effect. The

decision distorts the plain language of the Social Security Act, which expressly imposes the tax as an excise "with respect to having individuals in * * * employ." Liability for the tax is based upon the existence of the relationship of employment, without regard to whether the services rendered by the employee are in connection with production or manufacture. Both *Steward Machine Co.* v. *Davis, supra,* and *Helvering* v. *Davis,* 301 U. S. 619, make it clear that the tax is upon the relation existing between the employer and the employee. Nor is a tax "applicable directly" upon production or manufacture when it is laid upon other activities incident thereto, even if production or manufacture may absorb it or be affected by it. *Liggett & Myers Co.* v. *United States,* 299 U. S. 383.

B. In any event, there seems to be no warrant whatever for the further conclusion of the court below that taxes imposed, levied and collected by the State of Maryland are taxes "imposed by the Congress" simply because they may be deducted from the taxes imposed under Title IX of the Social Security Act. The tax "imposed by the Congress" is only the amount which is payable under that Act after all credits, deductions or other adjustments allowed by that Act in computing the ultimate amount to be paid have been given effect. Credit or other adjustment for taxes levied by States and foreign governments has long been allowed in determining the amount of Federal income and estate

taxes to be paid, but no one has ever supposed, and no court has suggested, so far as we find, that such State or foreign taxes were taxes imposed by the United States because the United States allowed a credit for such taxes in computing the amount which it would collect.

Batavia Mills, Inc. v. *United States*, decided by the Court of Claims on June 1, 1937, unreported,[1] which was relied upon by the court below on this branch of the case, is not pertinent. That case decided that processing taxes imposed and collected by the United States under the Agricultural Adjustment Act, c. 25, 48 Stat. 31, were recoverable by the one who paid them under a contract provision materially different from that involved here. There was no question respecting the authority which levied the tax. The only question there was whether a contractor who paid to the United States, but through a conduit, a tax admittedly imposed by the United States could recover the amount which he had paid to the United States through the conduit.

C. The decision below is of great general importance. Almost all government contracts since 1933 have contained provisions either identical with that here involved, or so similar as to present substantially the same question. It has not proved possible to make the extended search necessary to determine the precise number of contracts executed prior to the passage of the Social Security Act but under which

[1] The complete opinion appears in Appendix B, *infra*, pp. 14–19.

work was thereafter done. The War Department alone, however, states that approximately 4,000 potential claims may arise under contracts with language identical with that in Article 17 (3) of the contract in this case.

CONCLUSION

The decision below appears to be erroneous. It has decided a question of great general importance. Wherefore, we respectfully submit that this petition should be granted.

ROBERT H. JACKSON,
Solicitor General.

APRIL 1939.

APPENDIX A

Social Security Act, c. 531, 49 Stat. 620:

TITLE VIII—TAXES WITH RESPECT TO EMPLOYMENT

* * * * *

EXCISE TAX ON EMPLOYERS

SEC. 804. In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 811) paid by him after December 31, 1936, with respect to employment (as defined in section 811) after such date:

(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum.

* * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1004.)

COLLECTION AND PAYMENT OF TAXES

SEC. 807. (a) The taxes imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collections. * * * (U. S. C. Supp. IV, Title 42, Sec. 1007.)

DEFINITIONS

SEC. 811. When used in this title—

(a) The term "wages" means all remuneration for employment, including the cash value

of all remuneration paid in any medium other than cash; except that such term shall not include that part of the remuneration which, after remuneration equal to $3,000 has been paid to an individual by an employer with respect to employment during any calendar year, is paid to such individual by such employer with respect to employment during such calendar year.

(b) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

[Exceptions not pertinent.]

(U. S. C. Supp. IV, Title 42, Sec. 1011.)

TITLE IX—TAX ON EMPLOYERS OF EIGHT OR MORE

IMPOSITION OF TAX

SEC. 901. On and after January 1, 1936, every employer (as defined in Section 907) shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages (as defined in section 907) payable by him (regardless of the time of payment) with respect to employment (as defined in section 907) during such calendar year:

(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum;

(2) With respect to employment during the calendar year 1937 the rate shall be 2 per centum;

* * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1101.)

CREDIT AGAINST TAX

SEC. 902. The taxpayer may credit against the tax imposed by section 901 the amount of

contributions, with respect to employment during the taxable year, paid by him (before the date of filing his return for the taxable year) into an unemployment fund under a State law. The total credit allowed to a taxpayer under this section for all contributions paid into unemployment funds with respect to employment during such taxable year shall not exceed 90 per centum of the tax against which it is credited, and credit shall be allowed only for contributions made under the laws of States certified for the taxable year as provided in section 903. (U. S. C. Supp. IV, Title 42, Sec. 1102.)

CERTIFICATION OF STATE LAWS

SEC. 903. (a) The Social Security Board shall approve any State law submitted to it, within thirty days of such submission, which it finds provides that—

[Requirements not pertinent.]

(U. S. C. Supp. IV, Title 42, Sec. 1103.)

ADMINISTRATION, REFUNDS, AND PENALTIES

SEC. 905. (a) The tax imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collections. * * *

(U. S. C. Supp. IV, Title 42, Sec. 1105.)

DEFINITIONS

SEC. 907. When used in this title—

(a) The term "employer" does not include any person unless on each of some twenty days during the taxable year, each day being in a different calendar week, the total number of individuals who were in his employ for some

portion of the day (whether or not at the same moment of time) was eight or more.

(b) The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash.

(c) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

[Exceptions not pertinent.]

(U. S. C. Supp. IV, Title 42, Sec. 1107.)

APPENDIX B

The complete opinion in the case of *Batavia Mills, Inc.* v. *The United States*, decided by the Court of Claims on June 1, 1937, reads as follows:

No. 43176

BATAVIA MILLS, INC., *v.* THE UNITED STATES

Mr. Theodore B. Benson for plaintiff. Messrs. Charles E. Foster, Jr., and Henry O. Harriman were on the brief.

Mr. Guy Patten, with whom was Mr. Assistant Attorney General James W. Morris, for defendant. Messrs. Robert N. Anderson and Fred K. Dyar were on the brief.

This case having been heard by the Court of Claims, the Court, upon the stipulation of the parties and the evidence adduced, makes the following

SPECIAL FINDINGS OF FACT

1. Plaintiff is a corporation and on April 10, 1933, entered into a contract with the United States by which plaintiff agreed to sell and deliver to the United States at the Quartermaster Depot in Philadelphia, Pennsylvania, one million yards of shirting, cotton (oxford) khaki at $0.158 per yard, and the United States agreed to pay therefor the sum of $158,000. This contract, among other things, contained the following provision:

"It is understood that the prices set forth in this contract include as a part of the pur-

chase price to be paid for the supplies all sales-tax duties, imposts, revenues, excise or other taxes applicable to the supplies covered by this contract under any Federal law in force upon the date the bid upon which this contract is based was opened. If any change in the amount of such taxes is made by Congress or if any new taxes are made applicable to such supplies by Congress after the date of opening of the bid upon which this contract is based, the prices named in this contract will be increased or decreased accordingly."

A copy of the contract is attached to plaintiff's petition herein, marked "Exhibit I," and by reference made a part hereof.

2. The material described in the contract was furnished and delivered by plaintiff to defendant, accepted and approved by the government officials, and $158,000 paid to the plaintiff as provided by the contract.

3. Included in the supplies furnished and delivered by plaintiff under the aforesaid contract were 396,640 yards of cotton shirting upon which plaintiff paid an increased cost of $7,655.15 to Grosvenor-Dale Company, a Rhode Island Corporation of Providence, Rhode Island, this increased cost being $0.0193 per yard on the cloth by reason of floor stocks and/or processing taxes in that amount paid directly to the United States by the Grosvenor-Dale Company, the "Processor" (under the Agricultural Adjustment Act, approved May 12, 1933, as amended), on the first domestic processing of the cotton (a basic agricultural commodity under said Act), from which product said shirting was manufactured.

The Grosvenor-Dale Company, in manufacturing, spinning, and processing the cotton necessary to the manufacture of the shirting provided for in the contract, was compelled to pay and did pay to the Collector of Internal

Revenue at Providence, Rhode Island, the processing tax on 396,540 yards of shirting. This processing tax, at the rate of $0.0193 per yard, was paid to the Collector by the Grosvenor-Dale Company on the following dates, on the following yardage, in the following amounts, and included with other payments in the following totals:

Date	Yardage	Tax	Total payments in which included
9/30/33	117,627¼	$2,270.21	$23,389.97
10/13/33	92,630¾	1,787.77	17,194.70
10/23/33	90,043¼	1,737.83	25,000.00
10/28/33	96,338¾	1,859.34	22,441.15

4. Under the terms of its contract with the Grosvenor-Dale Company, plaintiff was required to reimburse the Grosvenor-Dale Company, and did, as aforesaid, reimburse said "Processor" the full amount of the processing tax, which payments were made by plaintiff to the Grosvenor-Dale Company, the "Processor," as follows:

October 2, 1933	$2,270.21
October 5, 1933	1,787.77
October 13, 1933	1,737.83
October 19, 1933	1,859.34

5. On October 9, 1933, plaintiff duly made claim and demand against the United States that the contract price for shirting be increased by the sum of $7,655.15, being the processing tax applicable to the cotton from which said shirting was manufactured under the Agricultural Adjustment Act, as amended, by filing claim and demand, under oath, with E. J. Heller, Captain, Quartermaster Corps, Philadelphia Quartermaster Depot, at Philadelphia, Pennsylvania.

On November 12, 1933, plaintiff duly filed with the Comptroller General of the United States its claim and demand that the contract price be increased by the sum of $7,655.15, pursuant to the terms of the contract. This claim was denied and rejected by the Comptroller General of the United States on February 5, 1934, upon the ground that said amount was not paid by plaintiff directly to the United States.

6. Plaintiff has tendered and delivered to defendant, for delivery to the Commissioner of Internal Revenue, a waiver duly signed by Grosvenor-Dale Company, the "Processor" heretofore mentioned, of any and all claims against the United States on account of floor stocks and/or processing taxes paid by the Grosvenor-Dale Company under the Agricultural Adjustment Act, as amended, to the extent of $7,655.15. This waiver has been deposited with defendant to be held in escrow pending the final determination of this case, and to be filed with the Commissioner of Internal Revenue in the event judgment is rendered herein in favor of plaintiff.

Defendant does not object to the form of the waiver.

CONCLUSIONS OF LAW

Upon the foregoing special findings of fact, which are made part of the judgment herein, the court decides, as a conclusion of law, that the plaintiff is entitled to recover the sum of $7,655.15.

It is therefore ordered and adjudged that the plaintiff recover of and from the United States the sum of seven thousand six hundred fifty-five dollars and fifteen cents ($7,655.15).

OPINION

GREEN, *Judge*, delivered the opinion of the court:

The plaintiff on April 10, 1933, entered into a contract by which it agreed to sell and deliver to the defendant a certain quantity of shirting and the United States agreed to pay for the same $158,000. The contract further provided in substance that the purchase price included all imposts applicable to the supplies to be furnished under any Federal law in force at the date when the contract was made, and that if any new taxes were subsequently made applicable to such supplies by Congress the price named in the contract would be increased accordingly.

The supplies were furnished by the plaintiff and $158,000 paid by the defendant. After the contract was made, by the passage of the Agricultural Adjustment Act, as amended, a processing tax was imposed upon the manufacturer from which the supplies were obtained amounting to $7,655.15 upon the "processing" of the goods so sold to plaintiff. The plaintiff's contract with the manufacturer corresponded with the provision in its contract with the United States and the plaintiff was required by the "processor" to pay this additional amount for the goods which it had purchased to fill the contract with the Government.

October 9, 1933, the plaintiff made a claim and demand against the defendant for this additional amount of $7,655.15. This claim was denied and rejected by the Comptroller General on the ground that said amount was not paid by plaintiff directly to the United States.

The ruling made by the Comptroller General cannot be sustained. This is not a suit

for the refund of taxes paid but an action based upon the provisions of a contract. The provisions of the law with reference to refunds of taxes collected under the Agricultural Adjustment Act have therefore no application. All of the matters necessary to establish plaintiff's claim under the contract are shown. After the contract was entered into a new and additional tax was imposed on the manufacturer from whom the contract supplies were purchased by plaintiff. The tax was passed on by the manufacturer and under the terms of plaintiff's contract with the manufacturer it was obliged to pay it. Defendant expressly agreed that the amount of the tax should be added to the purchase price. The right of plaintiff to recover the amount so paid is clear and judgment will be rendered accordingly.

WHALEY, *Judge;* WILLIAMS, *Judge;* LITTLETON, *Judge;* and BOOTH, *Chief Justice,* concur.

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CHARLES ELMORE CROPLEY
CLERK

No. 30

In the Supreme Court of the United States

OCTOBER TERM, 1939

THE UNITED STATES OF AMERICA, PETITIONER

v.

THE GLENN L. MARTIN COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE UNITED STATES

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OPINIONS BELOW

The opinion of the District Court (R. 10–14) is reported in 23 F. Supp. 262. The opinion of the Circuit Court of Appeals (R. 26–31) is reported in 100 F. (2d) 793.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 9, 1939 (R. 31). The petition for certiorari was filed April 8, 1939, and was granted May 1, 1939 (R. 32). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

A contract for the sale of materials by the respondent to the United States provided that the latter would reimburse the former for any taxes thereafter imposed by Congress "applicable directly upon production, manufacture, or sale" of the articles covered by the contract. Are taxes imposed by Titles VIII and IX of the Social Security Act and by the Maryland Unemployment Compensation Law "applicable directly upon production, manufacture, or sale" within the contract, and, if so, is the tax imposed by the Maryland Unemployment Compensation Law (for which a credit is allowed against the tax imposed by Title IX of the Social Security Act) imposed by Congress within the contract?

STATUTES INVOLVED

The relevant portions of Titles VIII and IX of the Social Security Act, and of the Maryland Unemployment Compensation Law, are set out in the Appendix, *infra*, pp. 20–24.

STATEMENT

Respondent brought this action under the Tucker Act (28 U. S. C. Sec. 41 (20)), in the District Court for the District of Maryland to recover $7,737.32 claimed to be due on a contract with the United States. The facts as stipulated (R. 4–7) and as found by the District Court (R. 10–14) may be summarized as follows:

On June 28, 1934, respondent and the United States entered into a contract for the sale by the former to the latter of certain aircraft and aircraft materials (R. 4, 10). The contract contained the following provision (R. 10–11):

> (3) It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge and other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein, and are paid by the contractor on the articles or supplies herein contracted for, then the price herein stipulated will be increased or decreased accordingly and any amount due the contractor as the result of such change will be charged to the Government and entered on vouchers as separate items.

On August 14, 1935, Congress enacted the Social Security Act (c. 531, 49 Stat. 620), and on December 17, 1936, Maryland enacted the Maryland Unemployment Compensation Law (Laws of Maryland, Extraordinary Session, December, 1936, c. 1). Thereafter, in 1936, respondent paid $766,962.82 and in 1937 paid $2,256.48 in wages for labor allocable to the performance of the contract (R. 5, 11).

Based on the wages so paid, the respondent, for 1936, paid $766.96 to the Federal Government under Title IX of the Social Security Act, and $6,902.67 to Maryland under that state's Unemployment Compensation Law (R. 5, 11). Under the same laws, the respondent for 1937 paid $27.07 to the Federal Government ($4.51 under Title IX and $22.56 under Title VIII), and $40.62 to Maryland (R. 5, 11). The total paid to both governments for these years is $7,737.32, of which $794.03 was paid to the Federal Government and $6,943.29 to Maryland.

Respondent billed the Government for the $7,737.32 paid to both federal and state governments, and, when payment was refused (R. 11, 24–25), brought this suit to recover the full amount. The District Court held that the taxes in question were not "applicable directly upon production, manufacture, or sale" (R. 13) and gave judgment for the United States. It therefore did not decide whether the taxes paid to the State of Maryland were "imposed * * * by the Congress". The Circuit Court of Appeals held against the United States on both questions, and reversed the judgment of the District Court, remanding the case for a new trial (R. 31–32). Since there is no dispute respecting the facts, the decision of the Circuit Court of Appeals is equivalent to a judgment for taxpayer for the full amount paid to both federal and state governments.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that taxes imposed by the Federal Social Security Act and by the Maryland Unemployment Compensation Act are "applicable directly upon production, manufacture, or sale" within the meaning of the contract.

2. In holding that the taxes levied and collected by the State of Maryland under its Unemployment Compensation Act are taxes "imposed * * * by the Congress" within the meaning of the contract.

3. In reversing the judgment of the District Court.

SUMMARY OF ARGUMENT

1. The social security taxes paid by the respondent were not "applicable directly upon production, manufacture, or sale", but upon the relation of employment. *Helvering* v. *Davis,* 301 U. S. 619; *Steward Machine Co.* v. *Davis,* 301 U. S. 548; *Carmichael* v. *Southern Coal Co.,* 301 U. S. 495.

Even if the taxes could be considered as applicable upon manufacture or production, clearly they were not "directly" so applicable. This is clear from the contract itself, for it cites sales and processing taxes as examples of taxes applicable directly to production and sale. Those taxes, in contrast to an employment tax, are fixed only in terms of the volume or value of production or sale, and thus are applicable "directly" upon these processes.

Taxes cannot be said to be "applicable directly" to production, simply because they affect labor costs.

2. In any event, the amounts paid to Maryland and credited against the Federal tax were not imposed by Congress. The tax imposed by Congress is only the amount which is payable under the Federal act after all credits, deductions or other adjustments allowed in computing the ultimate amount to be paid have been given effect.

Even if it could be said that the entire tax in this case was theoretically "imposed" by the Federal Government, liability for the payment of the tax so imposed was at all times contingent, and to the extent of the 90 per cent credit allowance was eliminated by the payments to the State of Maryland. The contract specifies that the tax so imposed must also have been paid.

ARGUMENT

I

THE SOCIAL SECURITY TAXES PAID BY THE RESPONDENT WERE NOT "APPLICABLE DIRECTLY UPON PRODUCTION, MANUFACTURE, OR SALE" WITHIN THE CONTRACT

The pertinent language of the contract provides that the prices stipulated therein shall be increased by the amounts of (R. 10–11)—

> * * * any sales tax, processing tax, * * * and other taxes * * * imposed * * * by the Congress subsequent to the date of this contract and made

> applicable directly upon production, manufacture, or sale of the supplies called for * * * and * * * paid by the contractor on the articles or supplies * * *

The taxes for which the respondent claims reimbursement under this provision were paid by respondent under (1) Titles VIII and IX of the Social Security Act, each of which levies an excise tax on employers "with respect to having individuals in his employ", the tax being measured by wages paid, and (2), the Maryland Unemployment Compensation Law, which requires employers to pay contributions "with respect to wages payable for employment", measured by such wages.

The constitutional validity of the taxes levied by Titles VIII and IX was upheld by this Court in, respectively, *Helvering* v. *Davis*, 301 U. S. 619, and *Steward Machine Co.* v. *Davis*, 301 U. S. 548, and the validity of the taxes levied by the Alabama Unemployment Compensation Act, which is of the same type as the Maryland law, were upheld in *Carmichael* v. *Southern Coal Co.*, 301 U. S. 495. In those cases the taxes are described as "upon the relation of employment", *Steward Machine Co.* v. *Davis, supra*, 578; *Helvering* v. *Davis, supra*, 645, or as on "the right to employ," *Carmichael* v. *Southern Coal Co., supra*, 508. Throughout the two former opinions the taxes are referred to as upon "pay rolls".

These taxes are not "applicable directly upon production, manufacture, or sale" within the contract provision. They are not "applicable" upon production, manufacture, or sale at all, but upon the relation of employment, or the pay roll. Liability for the taxes is based upon the existence of the relationship of employment, without regard to whether the services rendered by the employee are in connection with production or manufacture. For the same reason, the taxes were not "paid by the contractor on the articles * * * contracted for."[1]

Even if these pay roll taxes could be considered as applicable upon manufacture or production and as paid on the articles contracted for, clearly they are not applicable "directly" upon manufacture or production. That is apparent both from the meaning ordinarily attached to "directly" and from the context in which that word was used in the contract. The parties did not agree to make adjustment for all new federal taxes which might affect or increase the cost of production, but only for sales taxes, processing taxes, or other taxes which have *direct* application to production, manufacture or sale. It may, *arguendo,* be conceded that a tax on employment is a tax imposed with respect to manufacture or production because of the ordinary connection of employment with those processes.

[1] The word "on" in this connection obviously means "with respect to" or "in connection with".

But the requirement that the tax be "*directly* applicable" to production, manufacture or sale is read out of the contract if the normal dependence of manufacture upon employment be made the basis of decision. Respondent, for example, must pay Social Security taxes on salaries paid employees on vacation or sick leave. Yet it cannot be argued that the beneficial and recuperative effect for the employees is an element *directly* relating to production of the airplanes under the Government contract. This point is made clear by the contract itself, for it cites sales and processing taxes as the examples of taxes applicable directly to production and sale.[2] Those taxes, in contrast to an employment tax, are fixed only in terms of the volume or value of production or sale, and thus are applicable "directly" upon these processes.

The allocation to the contract with the Government of the taxes for which the petitioner seeks reimbursement involves a complicated accounting procedure in which not only direct but also indirect or overhead labor costs are allocated to the respective contracts (R. 5–6).[3] No challenge is made to

[2] The principle of *ejusdem generis* is, of course, applicable here. Cf. *Swift & Co.* v. *Columbia Ry., Gas & Electric Co.*, 17 F. (2d) 46 (C. C. A. 4th); *Alabama* v. *Montague*, 117 U. S. 602; *O'Connor* v. *Great Lakes Pipe Line Co.*, 63 F. (2d) 523.

[3] The method of accounting employed by respondent is as follows (R. 5–6): "That the Plaintiff, in determining the costs allocable to each contract in process of completion in its plant follows the following accounting procedure;

the correctness of the method of accounting. Indeed it is conceded to be in accord with good accounting practice. (See R. 7, 28.) But its complexity well illustrates the indirect relation of the Social Security taxes to manufacture or production. Indeed, since the overhead labor costs allocated to the Government contract vary according to the volume of other business, respondent's method of accounting makes it abundantly plain that the employment tax is paid only as an indirect consequence of manufacture or production for the Government.

The contract provision here in question does not provide that any tax which affected the costs or profits of the respondent was to be taken into account and adjustments in price made. The parties could have agreed to do business on a cost-plus basis, but they did not see fit to do so. Compare *Cramp & Sons Ship Co.* v. *United States*, 72 C. Cls.

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namely, a record is maintained of all direct labor costs on each contract and such direct labor costs are charged monthly to such contract. All costs other than direct labor (which includes all mechanical labor in the factory, such as tool and engineering labor) are charged to overhead on a monthly basis and each contract bears its share of overhead charges on a percentage basis, that percentage being the quotient of the total overhead for the particular month divided by the total direct labor costs for such month. For example, if the total direct labor costs and the total overhead costs of one month for all contracts amounted to $100,000.00 and $50,000.00, respectively, the monthly overhead charges allocable to each contract would be 50% of the direct labor costs charged to such contract."

146. Instead they agreed, in effect, that the contractor would bear subsequently enacted taxes, unless "applicable directly upon production, manufacture, or sale." Many government contracts do provide for an "equitable adjustment" in connection with change orders involving increases or decreases in labor, time, material, etc., and the Comptroller General has ruled that under such contracts the contractor is entitled to be reimbursed for social security taxes directly chargeable to change orders. 16 Comp. Gen. 672 (1937). On the other hand, he has ruled that a contractor is not, under a contractual provision substantially identical with that here in issue, entitled to reimbursement for social security taxes. 16 Comp. Gen. 790 (1937). The decision states (p. 791):

> * * * the so-called social security taxes are not taxes on coal, or on the production or sale of coal, but are taxes on the contractor "with respect to having individuals in his employ." It may be that such social security taxes increased your cost of production of coal from the mines, but the tax is not "applicable directly upon production, manufacture, or sale of" the coal required to be delivered under the contracts.

While precedents in other fields cannot be very persuasive as to the meaning of the term "applicable directly" in the contract provision here involved, a possible analogy may be found in the cases dealing with the supposed immunity of state instru-

mentalities from federal taxation. In *Liggett & Myers Co.* v. *United States*, 299 U. S. 383, a federal tax on tobacco sold to a state was upheld upon the ground that the tax was upon the manufacture of the tobacco, and not upon the sale; although the duty of payment was postponed until removal or sale, that tax imposed no "direct burden" upon the purchaser and "the effect upon the purchaser was indirect" (299 U. S. 383, 386). It seems to have been on this ground that the Court distinguished *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, in which it had held invalid a federal sales tax as applied to goods purchased by a municipality. So, too, in *Wheeler Lumber Co.* v. *United States*, 281 U. S. 572, 579, the Court sustained a transportation tax on the vendor who shipped f.o.b. to a county because "the transportation was not part of the sale but preliminary to it and wholly the vendor's affair." While we do not believe the *Indian Motocycle* case still to be good law, the *Liggett & Myers* and *Wheeler Lumber* cases are persuasive indications of the "indirect" relation of social security taxes to manufacture or sale.

Another analogy may be found in the interstate commerce cases. The states are powerless to impose a gross receipts tax or sales tax on interstate sales where the taxpayer is in danger of cumulative burdens. *Western Live Stock* v. *Bureau*, 303 U. S. 250, 255–256; *Gwin, Etc., Inc.* v.

Henneford, 305 U. S. 434, 439. Such a tax is considered to lay a "direct burden" on interstate commerce. See *Crew Levick Co.* v. *Pennsylvania,* 245 U. S. 292, 297. But none would argue that state social security taxes are forbidden by the commerce clause when the goods to be produced by the employees are intended for interstate delivery. See *Western Live Stock* v. *Bureau,* 303 U. S. 250, 259; *Utah Power & Light Co.* v. *Pfost,* 286 U. S. 165; *Federal Compress & W. Co.* v. *McLean,* 291 U. S. 17, 22; *Chassanoil* v. *Greenwood,* 291 U. S. 584.

The court below, in holding that the taxes here involved are "applicable directly" upon manufacture or production, cited the language of this Court in *Steward Machine Co.* v. *Davis,* 301 U. S. 548, 581, that:

> The power to tax the activities and relations that constitute a calling considered as a unit is the power to tax any of them. The whole includes the parts.

From that statement it drew the conclusion that the taxes are directly applicable upon the manufacture or production of the articles called for by the contract, since employment is necessary to both manufacture and production (R. 28.). But to say that in this case employment is indispensable to manufacture or production is not to say that a tax upon employment is directly applicable upon manufacture or production. Numerous other relationships or activities might be necessary to manufacture or production, such as the importation of goods from

abroad or the rental or ownership of property. But obviously a tax on those activities would not be directly applicable upon manufacture or production. If "applicable directly" means anything it means applicable to the activities of manufacture or production themselves. Taxes which might affect production or manufacture cannot be said to be "applicable directly" thereto, simply because of that effect.

II

THE AMOUNTS PAID TO MARYLAND AND CREDITED AGAINST THE FEDERAL TAX WERE NOT IMPOSED BY CONGRESS WITHIN THE MEANING OF THE CONTRACT

Of the $7,737.32 total taxes paid by the respondent for both of the years involved, only $794.03 was paid to the Federal Government; the balance of $6,943.29 was paid to the State of Maryland under Maryland's Unemployment Compensation Law, Laws of Maryland, Extraordinary Session, December, 1936, c. 1.

There seems to be no warrant whatever for the conclusion of the court below that taxes imposed, levied and collected by the State of Maryland are taxes "imposed * * * by the Congress" simply because they may be credited against the tax imposed by Title IX of the Social Security Act, up to 90 percent of the latter tax. The tax "imposed * * * by the Congress" is only the

amount which is payable under Title IX after all credits, deductions or other adjustments allowed in computing the ultimate amount to be paid have been given effect. Credit or other adjustment for taxes levied by states and foreign governments has long been allowed in determining the amount of federal income and estate taxes to be paid, but no one has ever supposed and no court has suggested, so far as we find, that such state or foreign taxes were taxes imposed by the United States because the United States allowed a credit for such taxes in computing the amount which it would collect.

Generally speaking, it might be said that the Federal Government was instrumental in the adoption of the entire body of social security laws, but it cannot be seriously argued that the taxes which the respondent paid into the treasury of the State of Maryland, pursuant to the Maryland statute, were imposed by the Federal Government. If Maryland had adopted its law under coercion by the Federal Government, it might be that the taxes levied by Maryland could, under a sufficiently determined theory of ultimate cause, be said to have been "imposed * * * by the Congress." But in *Steward Machine Co.* v. *Davis,* 301 U. S. 548, this Court held that Title IX did not coerce the states to adopt unemployment compensation. In that case, this Court recognized (p. 588) that many of the states had not enacted social security legisla-

tion, not because of a lack of sympathetic interest, but because of fear of placing themselves in a position of economic disadvantage as compared with neighboring states. It therefore remained for the Federal Government to protect against such fear, by providing for a tax contingent upon nonaction by the respective states, thus leaving the matter of social security relief fundamentally in the hands of the respective states. Though the state statute might well have been induced by the Federal Act, the taxpayer "pays in fulfilment of the mandate of the local legislature". *Steward Machine Co.* v. *Davis*, 301 U. S. 548, 589.

In the related case of *Carmichael* v. *Southern Coal Co.*, 301 U. S. 495, in discussing the relationship of the Alabama social security legislation to the Federal Social Security Act, this Court said (p. 526):

> Together the two statutes now before us embody a cooperative legislative effort by state and national governments, for carrying out a public purpose common to both, which neither could fully achieve without the cooperation of the other. The Constitution does not prohibit such cooperation.
>
> As the state legislation is not the product of a prohibited coercion, there is little else to which appellees can point as indicating a surrender of state sovereignty. As the opinion in the *Chas. C. Steward Machine Co.*

case points out, full liberty of action is secured to the state by both statutes.

Even if it could be said that the entire tax in this case was theoretically "imposed" by the Federal Government,[4] liability for the payment of the tax so imposed was at all times contingent, and, to the extent of the 90% credit allowance, the tax which was so imposed by the Federal Government was eliminated by the payments to the State of Maryland. The mere imposition in this broad sense was not what the parties contemplated, for the contract makes plain that they intended that the tax so imposed must also have been paid. The tax which, under this theory, the Federal Government imposed was never paid. Instead, the respondent paid a tax to the State of Maryland, whose legislature imposed that tax, and in turn received a credit to that extent on the federal tax.

Consideration of what the parties must have intended by the words "imposed * * * by the Congress" leads likewise to the conclusion that taxes levied by state laws were not meant to be covered. The apparent purpose of the provision

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[4] Section 902 (Title IX) of the Social Security Act provides:

"The taxpayer may credit against the tax *imposed* by section 901 the amount of contributions * * * paid by him * * * into an unemployment fund under a State law * * *". (Italics added.)

was that the Government should reimburse the contractor for certain types of subsequently imposed federal taxes which the Government itself received. It might not be necessary for the contractor to show that it paid the taxes directly to the Federal Government,[5] but it cannot be thought that it was intended that the Federal Government should reimburse respondent for taxes paid to some other government.

Batavia Mills v. *United States*, 85 C. Cls. 447, which was relied upon by the court below upon this point is not pertinent. The contract in that case provided, "* * * if any new taxes are made applicable to such supplies by Congress * * * the prices named in this contract will be increased or decreased accordingly." Thereafter Congress, by the Agricultural Adjustment Act, c. 25, 48 Stat. 31, imposed a processing tax which was paid on the contract materials by the manufacturer, and passed on by him to the contractor. There was no question that Congress had imposed the tax; the only question was whether the contractor was barred from recovering because he had not paid the tax directly to the United States. The Court held that he was not.

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[5] Cf. *Batavia Mills* v. *United States*, 85 C. Cls. 447, discussed below.

CONCLUSION

The decision of the court below is erroneous and should be reversed.

Respectfully submitted.

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SEPTEMBER 1939.

APPENDIX

Social Security Act, c. 531, 49 Stat. 620:

TITLE VIII—TAXES WITH RESPECT TO EMPLOYMENT

* * * * *

EXCISE TAX ON EMPLOYERS

SEC. 804. In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 811) paid by him after December 31, 1936, with respect to employment (as defined in section 811) after such date:

(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum.

* * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1004.)

COLLECTION AND PAYMENT OF TAXES

SEC. 807. (a) The taxes imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collections. * * *

(U. S. C. Supp. IV, Title 42, Sec. 1007.)

DEFINITIONS

SEC. 811. When used in this title—

(a) The term "wages" means all remuneration for employment, including the cash

value of all remuneration paid in any medium other than cash; except that such term shall not include that part of the remuneration which, after remuneration equal to $3,000 has been paid to an individual by an employer with respect to employment during any calendar year, is paid to such individual by such employer with respect to employment during such calendar year.

(b) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

[Exceptions not pertinent.]

(U. S. C. Supp. IV, Title 42, Sec. 1011.)

TITLE IX—TAX ON EMPLOYERS OF EIGHT OR MORE

IMPOSITION OF TAX

SECTION 901. On and after January 1, 1936, every employer (as defined in section 907) shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages (as defined in section 907) payable by him (regardless of the time of payment) with respect to employment (as defined in section 907) during such calendar year:

(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum;

(2) With respect to employment during the calendar year 1937 the rate shall be 2 per centum;

* * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1101.)

CREDIT AGAINST TAX

SEC. 902. The taxpayer may credit against the tax imposed by section 901 the amount of contributions, with respect to employment during the taxable year, paid by him (before the date of filing his return for the taxable year) into an unemployment fund under a State law. The total credit allowed to a taxpayer under this section for all contributions paid into unemployment funds with respect to employment during such taxable year shall not exceed 90 per centum of the tax against which it is credited, and credit shall be allowed only for contributions made under the laws of States certified for the taxable year as provided in section 903. (U. S. C. Supp. IV, Title 42, Sec. 1102.)

CERTIFICATION OF STATE LAWS

SEC. 903. (a) The Social Security Board shall approve any State law submitted to it, within thirty days of such submission, which it finds provides that—

[Requirements not pertinent.]

(U. S. C. Supp. IV, Title 42, Sec. 1103.)

ADMINISTRATION, REFUNDS, AND PENALTIES

SEC. 905. (a) The tax imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collections. * * * (U. S. C. Supp. IV, Title 42, Sec. 1105.)

DEFINITIONS

SEC. 907. When used in this title—

(a) The term "employer" does not include any person unless on each of some

twenty days during the taxable year, each day being in a different calendar week, the total number of individuals who were in his employ for some portion of the day (whether or not at the same moment of time) was eight or more.

(b) The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash.

(c) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

[Exceptions not pertinent.]

(U. S. C. Supp. IV, Title 42, Sec. 1107.)

Maryland Unemployment Compensation Law, Laws of Maryland; Extraordinary Session, December, 1936, c. 1:

CONTRIBUTIONS

7. (a) *Payment.*—

(1) On and after January 1, 1936, contributions shall accrue and become payable by each employer for each calendar year in which he is subject to this Act, with respect to wages payable for employment (as defined in section 19 (g)) occurring during such calendar year. Such contributions shall become due and be paid by each employer to the Board for the fund in accordance with such regulation as the Board may prescribe, and shall not be deducted, in whole or in part, from the wages of individuals in his employ.

(2) In the payment of any contributions, a fractional part of a cent shall be disregarded unless it amounts to one-half cent or more, in which case it shall be increased to 1 cent.

(*b*) *Rate of Contribution.*—

Each employer shall pay contributions equal to the following percentages of wages payable by him with respect to employment:

(1) Nine-tenths of 1 per centum with respect to employment during the calendar year 1936;

(2) One and eight-tenths per centum with respect to employment during the calendar year 1937;

(3) Two and seven-tenths per centum with respect to employment during the calendar years 1938 and thereafter.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1938.

UNITED STATES OF AMERICA,
Petitioner,

v.

THE GLENN L. MARTIN COMPANY,
A BODY CORPORATE,
Respondent.

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

JOHN T. KOEHLER,
Attorney for Respondent.

The Daily Record Co. Print, Baltimore.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1938.

No. 854.

UNITED STATES OF AMERICA,

Petitioner,

v.

THE GLENN L. MARTIN COMPANY,

A BODY CORPORATE,

Respondent.

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals (R. 43-48) is reported in 100 F. (2d) 793. The opinion of the District Court (R. 14-19) is reported in 23 F. Supp. 262.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered January 9, 1939 (R. 48). Notice of the filing of the petition for certiorari was served on counsel for the respondent on April 10, 1939. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial

Code, as amended by the Act of February 13, 1925 (c. 229, 43 Stat. 938: 28 U. S. C. A. sec. 347).

QUESTIONS PRESENTED.

1. Under a Government supply contract providing for an increase of the purchase price to reimburse the contractor for any "* * * other taxes or charges * * * imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacturer or sale of the supplies called for * * *" by the contract, is the contractor entitled to reimbursement for taxes subsequently imposed under Titles VIII and IX of the Social Security Act and allocated to the cost of performing this particular contract?

2. Are unemployment insurance taxes "* * * paid by the contractor * * *" to a state within the meaning of the "* * * other taxes or charges * * *" described in Question 1, such taxes being paid to a state pursuant to a law enacted after the adoption of the Social Security Act and neither increasing nor decreasing the total amount of unemployment insurance taxes (State and Federal) payable by the contractor after the Social Security Act became effective?

STATEMENT.

Most of the facts (none of which are in dispute) have been set forth in the petition (pp. 2-5). In addition, the District Court found (R. 16 and 23 F. Supp. 262, 263) that "The general purpose of the clause doubtless was to indemnify the contractor against increased cost of production due to increased taxes imposed by subsequent Acts of Congress, * * *" and the Circuit Court of Appeals stated (R. 46 and 100 F. (2d) 793, 795) that "* * * the provision was evidently inserted to protect

the contractor against loss arising from the imposition of new or additional federal taxes, which would increase his cost of production but could not be anticipated with an degree of accuracy; * * *".

REASONS FOR DENYING THE WRIT.

I.

No Important Question Is Presented.

This Court is asked to grant a writ of certiorari to review a decision of the Circuit Court of Appeals to the effect that a broad provision in a contract, the purpose of which was to indemnify the contractor against increased costs of production resulting from the imposition by Congress of new taxes which could not be anticipated when the contract was signed, included social security taxes paid by the respondent as an increased cost of labor engaged in the production of the supplies called for by the contract. The question so decided concerns only the meaning of the second sentence of Article 17 (3) of the contract under consideration as applied to a specific tax enacted after the contract was signed. As this brief points out, *infra*, p. 4, this sentence has been changed in subsequent contracts. It follows that the decision in this case is not a precedent for other or different taxes which might be imposed by Congress in the future. No important question of local, general or federal law is involved and no conflict of authority exists.

II.

The Asserted Basis For Granting Certiorari Is Too Indefinite To Be Substantial.

The petitioner asserts that the decision of the Circuit Court of Appeals is one of great importance *solely* because it is alleged that the provision is present in "Al-

most all Government contracts since 1933 * * *" and "The War Department alone, however, states that approximately 4,000 potential claims may arise * * *" (Petition pp. 8-9).

It is pertinent to observe that the second sentence of Article 17 (3) of the contract in question is applicable only to social security taxes paid under contracts signed before August 14, 1935, the date of enactment of the Social Security Act, in view of the fact that, in order to be recoverable, such taxes must have been " * * * imposed * * * by the Congress subsequent to the date of (the) contract." In addition, the second sentence of Article 17 (3) as contained in contracts subsequent to August 14, 1935, has been mo fied by Government draftsmen for the specific purpose of preventing the recovery of social security taxes paid into State unemployment compensation funds (see Appendix A). It follows that the broadest possible application of the decision of the Circuit Court of Appeals is limited to Government contracts signed between 1933 and August 14, 1935 which were not completed by January 1, 1936 and January 1, 1937, the effective dates of Titles IX and VIII respectively, of the Social Security Act (c. 531, 49 Stat. 620).

The petitioner seeks a further review of an adverse decision on the asserted ground that at least "* * * 4,000 potential claims may arise * * *". Aside from the fact that the scope of a decision is immaterial as a matter of law, it should be observed that the petitioner has failed to submit (1) an estimate of the amounts involved in these potential claims, (2) a statement of the number of suits, if any, which have been filed and which are based on such potential claims, and (3) an estimate of

the number and aggregate amount of such potential claims which will be barred by limitations during the current year (Section 24 (20) Judicial Code: 28 U. S. C. A. sec. 41 (20)).

Counsel for the Government has not contended that any other suit involving this question has been filed. Counsel for the respondent neither knows nor has been informed of any pending or prospective suit which involves the precise language of Article 17 (3) of the contract here under consideration, and knows or has been informed of but one suit involving language similar to that contained in this contract. In that case, the word "directly" does not appear. It is respectfully submitted, therefore, that this Court is asked to review a question involving nothing more than the interpretation of certain language in a Government contract which has not been shown to have far reaching significance.

III.

The Circuit Court of Appeals Decided Both Questions Correctly.

A. The District Court concluded that social security taxes were "* * * similar in nature to other burdens placed upon an employer by law for the safety or welfare of employees, such as required fire escapes on high buildings, and sanitary regulations for working conditions. All such humanitarian requirements clearly do actually increase manufacturing costs although they operate indirectly through overhead expense rather than directly, as would increased wages paid for the work done." (R. 17 and 23 F. Supp. 262, 264).

This confusion between capital expenditures and current expenses and the failure of the learned Court to distinguish between general overhead expenses and cur-

rent expenses allocable to a particular contract in course of completion led the Court to the incorrect conclusion that social security taxes on wages paid to individuals engaged in the performance of the contract were not applicable directly upon production or manufacture of the supplies called for by the contract. The Circuit Court of Appeals, without commenting upon the failure of the District Court to distinguish between capital expenditures and current expenses, approached the question from the correct point of view in the following language (R. 45, 46, and 100 F. (2d) 793, 795, 796):

> "And because the tax is one upon the relation of employment, it is argued that it cannot be a tax 'applicable directly' upon production or manufacture. We think, however, that, not this conclusion, but the contrary, is the one which logically follows. As the whole is the sum of all its parts, a tax applicable directly on one of the parts is necessarily applicable directly on the whole which comprises it. The manufacture or production of the supplies called for by the contract necessarily involves the employment of labor and the use of materials; and a tax applicable directly upon either is a tax applicable directly upon the manufacture or production itself. *No tax more directly applicable upon manufacture or production can be conceived, we think, than a payroll tax measured by wages paid to labor engaged therein.*" (Italics supplied.)
>
> * * * * * *
>
> "The learned judge below was of opinion that the tax operated 'indirectly through overhead expense rather than directly, as would increased wages paid for the work done'. But a payroll tax measured by the wages paid to produce an article burdens production and increases the cost thereof to the same extent and in substantially the same way as increased wages."

Proper weight was given to the word "directly" in the following language (R. 46 and 100 F. (2d) 793, 795):

> "The taxes, it will be noted, are to be applicable directly upon the 'manufacture, production or sale' of the articles, not directly upon the articles themselves; and this requirement of directness is satisfied where the tax is imposed on some essential element of 'manufacture, production or sale' in such way as to constitute a direct burden upon same. It excludes, of course, such taxes as do not directly burden 'manufacture, production or sale', such as income, excess profits and capital stock taxes."

B. The Circuit Court of Appeals decided the second question correctly by holding that contributions made by the respondent to the unemployment fund of the State of Maryland, and for which a credit was allowed against the tax imposed by Title IX of the Social Security Act to the extent of 90% of such tax, were nevertheless taxes imposed by Congress within the meaning of the contract. The Court declared (R. 47-48 and 100 F. (2d) 793, 796-797):

> "Even though the taxpayer was under legal obligation to pay the state tax to the state, the fact remains that that tax was imposed in connection with the general system brought into being by the federal Act and payment thereof was recognized as satisfying 90% of the obligation imposed by the federal tax. See Sections 903 and 904, 42 U. S. C. A. secs. 1103, 1104; *Steward Mach. Co. v. Davis,* 301 U. S. 548, 57 S. Ct. 883, 81 L. Ed. 1279, 109 A. L. R. 1293. If the state had not imposed a tax and established an unemployment fund complying with the requirements of the federal Act, the entire amount of the federal tax, without credit, would have been collected by the federal government and plaintiff would unquestionably have been entitled to recover same under the con-

tract provision. We think it is in no worse plight because the state has seen fit to comply with the provisions of the federal Act and thus receive 90% of the tax that it imposes."

In *Carmichael v. Southern Coal Co.*, 301 U. S. 495, 507, this Court declared:

> "By Section 902 of the Social Security Act, contributors to the state fund are entitled to credit their contributions *in satisfaction of the tax imposed on employers by the Social Security Act*, to the extent of 90% of the tax. See *Chas. C. Steward Machine Co. v. Davis*, decided this day, *post*, p. 548." (Italics supplied.)

Finally, it is to be noted that the second sentence of Article 17 (3) does not require that taxes imposed by Congress must have been paid by the contractor *to the United States* in order to be recoverable. The case of *Batavia Mills, Inc. v. United States*, 85 Ct. Cls. 447, 19 A. F. T. R. 1327, is directly in point.

CONCLUSION.

The Circuit Court of Appeals has correctly decided both questions, neither of which is of great general importance. Wherefore, it is respectfully submitted that the petition should be denied.

JOHN T. KOEHLER,
Attorney for Respondent.

April 20, 1939.

APPENDIX A.

In Orders and Regulations, Corps of Engineers, U. S. Army, Chapter VII (Contracts, Methods of Purchase and Claims), issued August 1, 1937, the following appears (pp. 57-58):

"(i) Federal, State, county, and municipal taxes. —If not contained in the standard forms of invitations for bids and contracts for the procurement of supplies, the following tax conditions will be included in all specifications for the procurement of supplies with proper reference thereto in the invitation form. Any tax conditions appearing in any of the supply forms in conflict therewith will be deleted.

Prices bid herein include any Federal tax heretofore imposed by the Congress which is applicable to the material on this bid. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress after the date set for the opening of this bid, and made applicable directly upon the production, manufacture, or sale of the supplies covered by this bid, and are paid *to the Government* by the contractor on the articles or supplies herein contracted for, then the prices named in this bid will be increased or decreased accordingly, and any amount due the contractor as a result of such change will be charged to the Government and entered on vouchers (or invoices) as separate items." (Italics supplied.)

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1939.

No. 30.

THE UNITED STATES OF AMERICA,
Petitioner,

v.

THE GLENN L. MARTIN COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

BRIEF FOR THE RESPONDENT.

JOHN T. KOEHLER,
WILLIAM A. FISHER, JR.,
Attorneys for Respondent.

The Daily Record Co. Print, Baltimore.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1939.

No. 30.

THE UNITED STATES OF AMERICA,
Petitioner,

v.

THE GLENN L. MARTIN COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

BRIEF FOR THE RESPONDENT.

OPINIONS BELOW.

The opinion of the District Court (R. 10-14) is reported in 23 F. Supp. 262. The opinion of the Circuit Court of Appeals (R. 26-31) is reported in 100 F. (2d) 793.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered January 9, 1939 (R. 31). The petition for cer-

tiorari was filed April 8, 1939, and was granted May 1, 1939 (R. 32). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (c. 229, 43 Stat. 938; 28 U. S. C. A. sec. 347).

QUESTIONS PRESENTED.

1. Under a Government supply contract providing for an increase of the stipulated purchase price to reimburse the contractor for any "* * * other taxes or charges * * * imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for * * *" by the contract, is the contractor entitled to reimbursement for taxes subsequently imposed under Titles VIII and IX of the Social Security Act and allocated to the cost of performing this particular contract?

2. Are unemployment insurance taxes "* * * paid by the contractor * * *" to a state within the meaning of the "* * * other taxes or charges * * *" described in Question 1, such taxes being paid to a state pursuant to a law enacted after the adoption of the Social Security Act and neither increasing nor decreasing the total amount of unemployment insurance taxes (state and federal) payable by the contractor after the Social Security Act became effective?

STATUTES INVOLVED.

The relevant portions of Titles VIII and IX of the Social Security Act, and of the Maryland Unemployment Compensation Law, are set out in the Appendix, *infra*, pp. 19-23.

STATEMENT.

Most of the facts (none of which are in dispute) have been set forth in the petitioner's brief (pp. 2-4). In addition, the facts as stipulated reveal that the contract was a standard form of Government contract (R. 4), and the petitioner, in its petition for a writ of certiorari, stated (p. 8) that "Almost all government contracts since 1933 have contained provisions either identical with that here involved, or so similar as to present substantially the same question."

SUMMARY OF ARGUMENT.

I. The social security taxes paid by the respondent constituted an additional cost of labor engaged in the performance of the contract. Since labor is an essential element of production and since the purpose of the contractual provision was to protect the respondent against loss arising from the imposition of new or additional federal taxes which would increase his cost of production, but which could not be anticipated, the payroll taxes so imposed and paid are clearly "* * * applicable directly upon production, manufacture, or sale of the supplies called for * * *" within the meaning of the contract. Since the language of a contract must be interpreted in the light of the circumstances existing at the time of its execution, it is erroneous to assume that the parties intended to give such language a technical construction wholly at variance with the purpose they sought to achieve.

II. The social security taxes paid by the respondent are recoverable in full since they were imposed by Congress and were paid by the respondent. The taxes imposed under Titles VIII and IX of the Social Security Act do not cease to be so imposed simply because Con-

gress gave taxpayers permission to pay a portion of such federal tax by means of a credit against similar taxes which might be payable under state unemployment compensation laws. In addition, the contract plainly did not require payment of any portion of the tax to the Federal Government as a condition precedent to recovery.

III. Since the contract was drafted in its entirety by the petitioner, the rule of construction which requires a contract to be interpreted most strongly against the party responsible for doubtful language should be applied here, and it is of no significance that the Federal Government happens to be the party against whom the rule is invoked.

ARGUMENT.

I.

THE SOCIAL SECURITY TAXES PAID BY THE RESPONDENT CONSTITUTED AN ADDITIONAL COST OF AN ESSENTIAL ELEMENT OF PRODUCTION OR MANUFACTURE AND WERE, THEREFORE, APPLICABLE DIRECTLY UPON PRODUCTION, MANUFACTURE OR SALE OF THE SUPPLIES CALLED FOR.

A. Article 17 (3) of the Contract Should Be Read in the Light of the Business and Accounting Principles Which Governed the Parties.

The contract between the petitioner and the respondent was signed on June 28, 1934, more than thirteen months before the Social Security Act was enacted (R. 4, 11). Article 17 (3) of the contract, after stating that the stipulated prices included "any Federal Tax heretofore imposed by the Congress which is applicable to the material called for" (R. 1-2, 10), provided further that:

> "If any sales tax, processing tax, adjustment charge and other taxes or charges are imposed or

changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change wil be charged to the Government and entered on vouchers as separate items."

The general purpose of this clause was, as the District Court stated (R. 12) "* * * to indemnify the contractor against increased costs of production due to increased taxes imposed by subsequent Acts of Congress * * *". The Circuit Court of Appeals stated (R. 29) that "* * * the provision was evidently inserted to protect the contractor against loss arising from the imposition of new or additional federal taxes, which would increase his cost of production but could not be anticipated with any degree of accuracy; and no tax could more clearly fall within the class of taxes which it was the purpose to provide against than an employment tax measured by the earnings paid to produce the articles which the contract called for." It follows that the language of the second sentence of Article 17 (3) was inserted in the contract partly to protect the contractor from being called upon to bear the burden of new or increased federal taxes which could not be anticipated (R. 29), and partly to prevent the contractor from submitting an excessive bid, the justification for such bid being that an allowance for a possible increase in present taxes or the enactment of new taxes would be a necessary protective measure.

Since there is no dispute concerning the purpose of Article 17 (3), this Court is asked to determine whether or not, with respect to social security taxes, the language used by the parties to effect that purpose falls short of the mark. In considering this question, it seems erroneous to assume, as the petitioner does, that the language of a business contract must be construed in the light of finely-drawn legal distinctions among various types of excises. To do so is to assume that the parties to the contract were aware of such distinctions and acted accordingly. It would seem to be more reasonable and more in accordance with the facts to assume that a business contract should be interpreted in accordance with principles of good business practice and sound accounting procedure, since both parties must be deemed to have signed the contract with such principles in mind. This is particularly true in the present case since the methods of accounting employed by the respondent conformed to a standard code of accounting approved by the petitioner (R. 7), were subjected to a daily examination during the period of performance (R. 7) and stand approved at the present time (Br. 9-10). It follows that the language of Article 17 (3) should be read in the light of the business and accounting principles which governed the parties thereto. *Miller v. Robertson*, 266 U. S. 243; *Canal Co. v. Hill*, 82 U. S. 94; *Gilmartin v. Princeton Bank & Trust Co.*, 80 F. (2d) 130 (C. C. A.-4). If the contract as so interpreted reveals that the respondent was to be protected against new taxes subsequently imposed by Congress, which, in accordance with sound business principles, increased its direct production costs, then such protection should not be denied.

B. As a Matter of Accounting, Social Security Taxes Are Applicable Directly Upon Production Because They Constitute an Additional Cost of Labor.

Under the method of accounting employed by the respondent, social security taxes paid by it on the direct labor engaged in the performance of the contract amounted to $5,616.06, while such taxes paid on overhead labor so engaged amounted to $2,131.26, making a total of $7,737.32, the amount for which suit was brought (R., 6, 28). It is conceded that this allocation was in accordance with correct accounting principles (Br. 10, R. 28). The Circuit Court of Appeals decided (R. 28) that the social security taxes paid on both direct and indirect labor engaged in the performance of the contract were recoverable. The petitioner does not assert, in its "Specification of Errors to be Urged" (Br. 5), or elsewhere, that the lower Court erred in so holding and does not claim that, within the meaning of Article 17 (3) of the contract, any distinction should be drawn between social security taxes paid on direct labor and like taxes paid on indirect labor. It follows that the sole question before this Court is whether or not the words "* * * other taxes or charges * * * made applicable directly upon production, manufacture, or sale of the supplies called for * * *" include payroll taxes on labor engaged in the performance of the contract.

The respondent's method of accounting required *all* taxes, except federal and state income taxes, to be included in overhead (R. 7). Consequently sales taxes, processing taxes and, following their subsequent enactment, social security taxes were all accorded the same accounting treatment. Article 17 (3) of the contract designates sales and processing taxes as examples of ex-

cise taxes "applicable directly upon production, manufacture, or sale" and the petitioner admits, of course, that such taxes would clearly be recoverable (Br. 9).[1] In determining the meaning of the words "applicable directly," it is, therefore, of no significance that the respondent was required to charge all excises, including social security taxes, to overhead and the petitioner does not so contend. To assert otherwise would be to deny the recovery of *any* excise tax imposed by Congress and would strike Article 17 (3) in its entirety from the contract. It follows that the "complicated accounting procedure" (Br. 9) of the respondent which "illustrates the indirect relation of the Social Security taxes to manufacture or production" (Br. 10) was equally applicable to taxes admitted to be "applicable directly upon production, manufacture, or sale".

The difficulties encountered by the petitioner in construing the words "applicable directly" arise, it is submitted, from a failure to interpret such words in accordance with accepted principles of business practice and accounting procedure. Cost accountants agree that the basic elements of the costs of production (manufacturing costs) are material, labor and other expenses, and that

[1] The petitioner does not specify what taxes other than sales and processing taxes might be recovered and relies upon the principle of *ejusdem generis* to limit the words "other taxes or charges" (Br. 9). However, the rule of *ejusdem generis* is merely a rule of construction to ascertain intention when such intention cannot be gathered from the context. *Helvering v. Stockholms Enskilda Bank*, 293 U. S. 84, 89. It is only an illustration of the broader maxim *noscitur a sociis* and, where applicable, does not require that the general terms following the specification of particular things or classes be rejected, but that such terms shall be deemed to include all things or classes which, though not enumerated, fall within such classification. *R. E. Durall Co. v. W., B. & A. Electric R. R. Co.*, 51 F. (2d) 566, 570 (C. C. A. 4); *Williston on Contracts* (1936 Ed.) sec. 619, citing *Swift & Co. v. Columbia Ry. etc. Co.*, 17 F. (2d) 46 (C. C. A. 4); and *Cleveland Transit Co. v. Consolidated Gas etc. Co.*, 55 F. (2d) 211 (C. C. A. 4). Any excise tax, therefore, applicable directly upon production manufacture or sale, falls within the words "other taxes or charges".

each of these elements is, in turn, divided into *direct* and *indirect* costs.[2] The distinction between direct and indirect costs of production is that "* * * the former are incurred directly for and are chargeable to specific cost units (material, labor and expense) while the latter are incurred for the productive process as a whole and must be spread over the cost units involved on some more or less arbitrary basis."[3] (Matter in parenthesis supplied.)

Viewed in the light of the foregoing principles, the meaning of the words "applicable directly upon production, manufacture, or sale" becomes clear. Processing taxes on materials, for instance, are *direct* expenses which increase or follow the direct cost of such materials and are, therefore, "appplicable directly" upon such cost. Capital stock taxes and stamp taxes, similar to light, heat, insurance and costs of a like nature, are examples of *indirect* expenses which do not increase or follow direct material or labor costs and are, therefore, applicable only indirectly upon production costs.[4] Income and excess profits taxes are neither directly nor indirectly applicable to production costs, since they are imposed on earnings and are not an item of cost (R. 7).

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[2] *Reitell—"Cost Accounting—Principles and Methods"*, pp. 24-28 (International Textbook Co.—1933); *Accountants Handbook*, p. 1282 (2nd Ed.) Ronald Press—1932.

[3] *Accountants Handbook op. cit.* p. 1282. A *direct* material cost or charge is the raw material from which the finished product is made; an *indirect* material cost or charge is material necessary to the processes of manufacture, but not forming a part of the finished product, i. e., operating supplies used in production. Similarly, *direct* expenses are "* * * expenditures which pertain to or follow either direct material or direct labor, so as in reality to be a part of either the one or the other * * *", while *indirect* expenses are expenditures which "* * * arise from the necessity of providing a place to work in, power to operate machines, and other requirements of a similar nature." *Reitell—op. cit.* p. 26.

[4] *Holmes—"Auditing—Principles and Procedure"*, p. 374 (Business Publications, Inc. 1939).

The distinction between processing taxes (direct expenses which increase direct material costs) and capital stock taxes (indirect expenses which do not increase direct material costs but are chargeable only to indirect expenses as manufacturing overhead) illustrates the proper meaning to be given to the words "applicable directly upon production, manufacture, or sale". Social security taxes are clearly *direct* expenses which increase labor costs.[5] The concensus of accounting opinion is that payroll taxes on labor are an additional cost of that labor (direct expense) and are not to be considered a cost of facilities and services for making the labor more effective (indirect expense).[6] It follows that a tax which is sufficiently direct in nature to be regarded by accountants as a part of an admittedly direct charge (labor) to production or manufacture is "applicable directly" upon such production or manufacture. Consequently, *both* processing taxes and social security taxes are *direct* expenses which are properly included in, and form a part of, material and labor costs. To admit that the former is "applicable directly upon production, manufacture, or sale" and, at the same time, to assert that the latter is not so applicable is to do violence to the principles of accounting which governed the parties to the contract.

It is well settled that courts of law will recognize and apply standard principles of accounting in order to determine the proper meaning to be attributed to words

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[5] *Sherwood-Culey—"Auditing Theory and Practice"*, pp. 372, 445 (South-Western Publishing Co. 1939); *Neuner—"Cost Accounting"*, p. 190, (Business Publications, Inc. 1938).

[6] *National Association of Cost Accountants Bulletin*, Vol. XVIII, No. 24, pp. 1376-77 (1937). In a subsequent report (N. A. C. A. Bulletin, Vol. XX, No. 3, pp. 187, 188, 193 (1938)), the Association stated that examination of the accounting treatment of payroll taxes by 639 manufacturing companies revealed that the great majority of such companies treated payroll taxes as a direct charge to labor.

which have acquired a definite business significance. *Eisner v. Macomber*, 252 U. S. 189, 209; *Bowers v. Kerbaugh-Empire Co.*, 271 U. S. 170; *Dayton Power & Light Co. v. Public Utilities Commission*, 292 U. S. 290; *Lindheimer v. Illinois Telephone Co.*, 292 U. S. 151, 168; *Lone Star Gas Co. v. Texas*, 304 U. S. 224. This would seem to be particularly true where, as in the present case, such principles of accounting were, in effect, incorporated in the contract (R. 7) and where the application of such principles was subject to the daily scrutiny and approval of the petitioner during the entire period of performance (R. 7).

C. As a Matter of Law, Social Security Taxes Are Applicable Directly Upon Production Because They Constitute an Additional Cost of Labor.

The petitioner refuses to include social security taxes within the scope of the contractual indemnity against future excise taxes on the ground that the nature of this particular type of excise (a tax on the relation of employment) prevents it from being either *directly or indirectly* applicable upon production, manufacture or sale (Br. 8). This argument was characterized by the District Court as "* * * a construction of the wording which seems very narrow and literal" (R. 12) and was unqualifiedly rejected by the Circuit Court of Appeals (R. 28). The petitioner admits that, if this argument is sound, social security taxes "* * * are not 'applicable' upon production, manufacture or sale at all * * *" (Br. 8).

The last sentence of the preceding paragraph illustrates that a failure to give the words "applicable directly" the meaning accorded them by the parties may result in an interpretation which clearly lacks plausibility.

Just as the words of a statute must be read in their plain popular meaning (*Woolford Realty Co. v. Rose*, 286 U. S. 319), so the words of a contract must be given the meaning the parties obviously intended. *United States Fidelity & Guaranty Co. v. French Mutual General Society*, 212 Fed. 620 (C. C. A. 4). To say that a tax which directly increases the cost of production or manufacture is not applicable to (i. e., does not affect) that cost is to do violence to the normal meaning attributable by business men to the words "applicable directly".

This Court has already decided that a tax upon the relation of employment is none the less a tax applicable upon production. In *Carmichael v. Southern Coal Co.*, 301 U. S. 495, 524-525, this Court, speaking through Mr. Justice STONE, stated:

> "The Alabama legislature may have proceeded upon the view, for which there is abundant authority, that the causes of unemployment are too complex to admit of a meticulous appraisal of employer responsibility. It may have concluded that unemployment is an inseparable incident of modern industry, with its most serious manifestations in industrial production; that employees will be best protected, and that *the cost of the remedy, at least until more accurate and complete data are available, may best be distributed, by imposing the tax evenly upon all industrial production, and in such form that it will be added to labor costs* which are ultimately absorbed by the public in the prices which it pays for consumable goods." (Italics supplied.)

It follows that a tax may still be "applicable directly upon production, manufacture, or sale" within the meaning of the contract in this case, even though the nature of such tax has been stated to be "upon the relation of employment."

The petitioner, in searching for a construction of the words "applicable directly" apart from the accepted meaning ascribed to them in this brief, enters the fields of federal taxation and interstate commerce (Br. 11-13). Although the present case is not a suit for the refund of taxes, but is simply an action for breach of a contract (R. 1), it is perhaps pertinent to observe that the case of *Liggett & Myers Co. v. United States*, 299 U. S. 383 (Br. 12) is authority for the proposition that a tax on tobacco prior to its sale to a state imposes only an indirect burden on the state. This burden was held to be indirect because the tax was imposed, not on the state, but on the manufacturer who sold it the tobacco. Had the respondent sought to recover payroll taxes paid by a manufacturer on goods sold to the respondent, the cited case might have some bearing here. It can, however, have no appplication where the tax is imposed directly upon a manufacturer who later sues to recover it.

The interstate commerce cases cited by the petitioner (Br. 12-13) hold that a tax on a privilege or franchise "equal to" or "measured by" gross receipts amounts to a direct tax on such receipts, regardless of the wording of the particular statute. Consequently, if such gross receipts are derived from interstate commerce, the tax is invalid as a direct burden upon such commerce. It would seem, therefore, that the cited cases are authority for the proposition that this Court will consider the nature and effect of a tax regardless of the particular language in which it may have been couched. As was said in *Crew Levick Co. v. Pennsylvania*, 245 U. S. 292, 294:

> "As in other cases of this character, we accept the decision of the state court of last resort, respecting the proper construction of the statute, but are in

> duty bound to determine the questions raised under the Federal Constitution *upon our own judgment of the actual operation and effect of the tax, irrespective of the form it bears or how it is characterized by the state courts.*" (Italics supplied.)

It is respectfully submitted that this language is equally applicable to the facts of the instant case and that a tax "upon the relation of employment" does not cease to be a tax which directly affects, or is "applicable directly" upon, production or manufacture by increasing the cost of an essential element thereof. It follows that the social security taxes sought to be recovered fall squarely within the language of Article 17 (3), that the words "applicable directly upon production" include all taxes which directly increase production costs and exclude all others, and, finally, that such words should be read in the light of the meaning attributable to them by the parties and not in the light of technical differences attributable to various types of excises.

II.

THE SOCIAL SECURITY TAXES PAID BY THE RESPONDENT ARE RECOVERABLE IN FULL SINCE SUCH TAXES WERE IMPOSED BY CONGRESS AND WERE PAID BY THE RESPONDENT.

The petitioner urges (Br. 14-18) that the parties did not intend the respondent to be reimbursed for any taxes imposed by Congress unless such taxes were actually paid to the Federal Government. This argument loses sight of the fact that the contract provided for the recovery of "* * * other taxes or charges * * * imposed or changed by the Congress subsequent to the date of this contract and * * * paid by the Contractor on the articles or supplies herein contracted for * * *". It will be noticed that payment "to the Federal Govern-

ment" is not a prerequisite to recovery. *Batavia Mills, Inc., v. United States*, 85 Ct. Cls. 447, is directly in point.

The argument pressed here by the petitioner was so well answered by the Circuit Court of Appeals that the respondent feels that any attempt to parallel the cogent reasoning of the lower Court would be ineffectual. Accordingly, the second portion of the opinion of the Circuit Court of Appeals is here reproduced in full. Speaking for the Court, Judge PARKER stated (R. 30-31):

> "Coming to the second question, i. e., whether the portion of the tax paid to the State of Maryland and credited against the tax due under the Act to the federal government falls within the meaning of the clause of the contract under consideration, it is to be noted that this portion, as well as the remainder, falls squarely within the language used. The entire amount of the tax was 'imposed' by Congress and was 'paid by the contractor.' That a part of it was paid with the consent of Congress to the State of Maryland and credited against the amount which would otherwise have been due under the Act, would seem to be immaterial. A very similar question was before the Court of Claims in *Batavia Mills, Inc., v. United States* (decided June 1, 1937, but unreported). There, a processing tax on cotton yarn had been paid by the manufacturer of cotton cloth to the selier of the yarn pursuant to the terms of a contract under which the yarn was purchased. The manufacturer of the cloth had sold it to the government under a contract providing that the price should be increased by the amount of any new taxes made applicable by Congress to the supplies to be furnished after the date of the bid. In holding that the amount of the tax so paid might be recovered by the manufacturer of the cloth, who had not paid it to the government but to the processor of the yarn, the court said:

"'This is not a suit for the refund of taxes paid but an action based upon the provisions of a contract. The provisions of the law with reference to refunds of taxes collected under the Agricultural Adjustment Act have theretofore no application. All of the matter necessary to establish plaintiff's claim under the contract are shown. After the contract was entered into a new and additional tax was imposed on the manufacturer from whom the contract supplies were purchased by plaintiff. The tax was passed on by the manufacturer and under the terms of plaintiff's contract with the manufacturer it was obliged to pay it. *Defendant expressly agreed that the amount of the tax should be added to the purchase price.* The right of plaintiff to recover the amount so paid is clear and judgment will be rendered accordingly.'

"The Federal Social Security taxes were imposed by Congress as part of a comprehensive plan in which the states were expected to participate. That the states might be induced to do this, it was provided in the Act that the taxpayer might credit against the tax imposed by it any contributions paid by him into a state unemployment fund, to an amount not exceeding 90% of the amount of the tax under the federal Act. *This, of course, was no more than permission to the taxpayer to pay to the state 90% of the tax imposed by the Act and to credit same as a deduction on the federal tax;* and where the plaintiff availed itself of this privilege, paying a portion of the tax imposed to the state and claiming credit therefor under the Act, we think that it comes within the protection of the spirit as well as the language of the clause in the contract here-under consideration. *Even though the taxpayer was under legal obligation to pay the state tax to the state, the fact remains that that tax was imposed in connection with the general system*

brought into being by the federal Act and payment thereof was recognized as satisfying 90% of the obligation imposed by the federal tax. See Sections 903 and 904; *Steward Mach. Co. v. Davis*, 301 U. S. 548. If the state had not imposed a tax and established an unemployment fund complying with the requirements of the federal Act, the entire amount of the federal tax, without credit, would have been collected by the federal government and plaintiff would unquestionably have been entitled to recover same under the contract provision. We think it is in no worse plight because the state has seen fit to comply with the provisions of the federal Act and thus receive 90% of the tax that it imposes. *The clause of the contract was intended to protect plaintiff against new taxes to be imposed by the federal government. It should not be denied this protection because that government permits a portion of the taxes imposed to be paid to the states under a general scheme for state and federal cooperation.*" (Italics supplied).

That this Court is of the opinion that social security taxes paid under State unemployment compensation laws are paid to discharge a tax imposed by the Federal Government is evident from *Carmichael v. Southern Coal Co.*, 301 U. S. 495. In that case this Court declared (p. 507):

> "By §902 of the Social Security Act, contributors to the state fund are entitled to credit their contributions *in satisfaction of the tax imposed on employers by the Social Security Act*, to the extent of 90% of the tax. See *Chas. C. Steward Machine Co. v. Davis*, decided this day, post, p. 548" (Italics supplied).

III.

IF ANY DOUBTS EXIST CONCERNING THE MEANING OF ARTICLE 17 (3) THEY SHOULD BE RESOLVED AGAINST THE PETITIONER.

The contract here involved was a standard form of government supply contract and was admittedly drafted by the petitioner. The rule of construction which requires a contract, in case of doubt concerning the meaning of its language, to be construed most strongly against the party drafting it applies to the Federal Government as fully as if the Government were an individual. As this Court stated in *Reading Steel Casting Co. v. United States*, 268 U. S. 186, 188, a case in which the United States was a contracting party:

> "The contract is to be construed and the rights of the parties are to be determined by the application of the same principles as if the contract were between individuals."

To the same effect see *Garrison v. United States*, 7 Wall. 688, 690; *United States v. Smith*, 4 Otto 214, 217; *Marietta Mfg. Co. v. United States*, 73 Ct. Cls. 528, 546.

CONCLUSION.

The decision of the Court below is correct and should be affirmed.

Respectfully submitted,

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APPENDIX.

Social Security Act, c. 531, 49 Stat. 620:

TITLE VIII—TAXES WITH RESPECT TO EMPLOYMENT.

* * * * * * *

EXCISE TAX ON EMPLOYERS.

SEC. 804. In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 811) paid by him after December 31, 1936, with respect to employment (as defined in section 811) after such date:

(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum.

* * * * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1004).

COLLECTION AND PAYMENT OF TAXES.

SEC. 807 (a). The taxes imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collection. * * *

(U. S. C. Supp. IV, Title 42, Sec. 1007).

DEFINITIONS.

SEC. 811. When used in this title—

(a) The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash; except that such term shall not include that part of the remuneration which, after remuneration equal to $3,000 has been

paid to an individual by an employer with respect to employment during any calendar year, is paid to such individual by such employer with respect to employment during such calendar year.

(b) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

(Exceptions not pertinent).

(U. S. C. Supp. IV, Title 42, Sec. 1011).

TITLE IX—TAX ON EMPLOYERS OF EIGHT OR MORE.

Imposition of Tax.

SECTION 901. On and after January 1, 1936, every employer (as defined in section 907) shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages (as defined in section 907) payable by him (regardless of the time of payment) with respect to employment (as defined in section 907) during such calendar year:

(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum;

(2) With respect to employment during the calendar year 1937 the rate shall be 2 per centum;

* * * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1101).

Credit Against Tax.

SEC. 902. The taxpayer may credit against the tax imposed by section 901 the amount of contributions, with respect to employment during the taxable year, paid by him (before the date of filing his return for the taxable year) into an unemployment fund under a State law. The total credit allowed to a taxpayer under this

section for all contributions paid into unemployment funds with respect to employment during such taxable year shall not exceed 90 per centum of the tax against which it is credited, and credit shall be allowed only for contributions made under the laws of States certified for the taxable year as provided in section 903.

(U. S. C. Supp. IV, Title 42, Sec. 1102).

CERTIFICATION OF STATE LAWS.

SEC. 903 (a). The Social Security Board shall approve any State law submitted to it, within thirty days of such submission, which it finds provides that—

(1) All compensation is to be paid through public employment offices in the State or such other agencies as the Board may approve;

(2) No compensation shall be payable with respect to any day of unemployment occurring within two years after the first day of the first period with respect to which contributions are required;

(3) All money received in the unemployment fund shall immediately upon such receipt be paid over to the Secretary of the Treasury to the credit of the Unemployment Trust Fund established by section 904;

(4) All money withdrawn from the Unemployment Trust Fund by the State agency shall be used solely in the payment of compensation, exclusive of expenses of administration;

(5) Compensation shall not be denied in such State to any otherwise eligible individual for refusing to accept new work under any of the following conditions: (A) If the position offered is vacant due directly to a strike, lockout, or other labor dispute; (B) if the wages, hours, or other conditions of the work offered are substantially less favorable to the individual than those prevailing for similar work in the locality; (C) if as a condition of being employed the individual would be

required to join a company union or to resign from or refrain from joining any bona fide labor organization;

(6) All the rights, privileges, or immunities conferred by such law or by acts done pursuant thereto shall exist subject to the power of the legislature to amend or repeal such law at any time.

The Board shall, upon approving such law, notify the Governor of the State of its approval.

(U. S. C. Supp. IV, Title 42, Sec. 1103).

ADMINISTRATION, REFUNDS, AND PENALTIES.

SEC. 905 (a). The Tax imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collections. * * * (U. S. C. Supp. IV, Title 42, Sec. 1105).

DEFINITIONS.

SEC. 907. When used in this title—

(a) The term "employer" does not include any person unless on each of some twenty days during the taxable year, each day being in a different calendar week, the total number of individuals who were in his employ for some portion of the day (whether or not the same moment of time) was eight or more.

(b) The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash.

(c) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

(Exceptions not pertinent).

(U. S. C. Supp. IV, Title 42, Sec. 1107).

Maryland Unemployment Compensation Law, Laws of Maryland, extraordinary Session, December, 1936, c. 1:

CONTRIBUTIONS.

7. (a) Payment.—

(1) On and after January 1, 1936, contributions shall accrue and become payable by each employer for each calendar year in which he is subject to this Act, with respect to wages payable for employment (as defined in section 19 (g) ocurring during such calendar year. Such contributions shall become due and be paid by each employer to the Board for the fund in accordance with such regulation as the Board may prescribe, and shall not be deducted, in whole or in part, from the wages of individuals in his employ.

(2) In the payment of any contributions, a fractional part of a cent shall be disregarded unless it amounts to one-half cent or more, in which case it shall be increased to 1 cent.

(b) Rate of Contribution.—

Each employer shall pay contributions equal to the following percentages of wages payable by him with respect to employment:

(1) Nine-tenths of 1 per centum with respect to employment during the calendar year 1936;

(2) One and eight-tenths per centum with respect to employment during the calendar year 1937;

(3) Two and seven-tenths per centum with respect to employment during the calendar years 1938 and thereafter.

P. 2.

SUPREME COURT OF THE UNITED STATES.

No. 30.—October Term, 1939.

The United States of America, Petitioner, *vs.* The Glenn L. Martin Company.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Fourth Circuit.

[November 6, 1939.]

Mr. Justice Black delivered the opinion of the Court.

We must determine whether a contract to purchase certain aircraft and aircraft material from respondent required the United States to increase the stipulated price by the amount of Social Security taxes paid by respondent.

June 28, 1934, the War Department and respondent, a Maryland manufacturer, made the contract, providing—

"It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for then the price herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

With respect to payrolls of employees alleged to have been engaged in fulfilling this contract during 1936 and 1937, respondent paid $794.03 in Federal Social Security taxes and $6,943.29 under the State of Maryland's Unemployment Compensation Law. Both the Federal tax and Maryland's tax were levied "subsequent to the date of this contract." Respondent claims that both the Maryland Unemployment Compensation taxes[1] and the Federal Social Se-

[1] Laws of Maryland, extraordinary session, Dec. 1936, c. 1.

curity taxes[2] were "imposed . . . by . . . . Congress" and were of the type for which the contract provided extra compensation.

Rejecting respondent's construction of the contract, the District Court held that no part of the taxes paid by respondent served to increase the liability of the Government on its contract.[3] The Circuit Court of Appeals reversed[4] and we granted certiorari.[5]

Obviously, the seller fixed its stipulated prices so as to provide a margin of profit over Federal taxes for which it might at the time of the contract be responsible on the particular "material" sold. This clearly appears from the governing provision's opening declaration that "the prices herein stipulated include any Federal tax heretofore imposed by Congress which is applicable to the material called for under the terms of this contract." But, without more, future increases in Federal taxes "applicable to the material" might have substantially affected the margin of profit which the contract was calculated to insure. Against the contingency of increase in Federal taxes applicable to the "material" purchased, the Government undertook to compensate the seller for payment of future Federal taxes "on the articles or supplies contracted for" should Congress levy any sales tax, processing tax or other tax "applicable directly upon production, manufacture or sale of the articles . . . contracted for . . . . ."

But the Social Security Act[6] imposes upon every employer "an excise tax with respect to having individuals in his employ." And employment in that Act "means any service, of whatever nature, performed within the United States by an employee for an employer . . . " with exceptions not material here. This excise has been represented as one levied "upon the relation of employment"[7]

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[2] 49 Stat. 620, 637.

[3] 23 F. Supp. 262.

307 US 618

[4] 100 Fed. (2d) 793.

[5] U. S. . The government's petition for certiorari set out that "Almost all government contracts since 1933 have contained provisions either identical with that here involved, or so similar as to present substantially the same question. . . . The War Department alone . . . states that approximately 4,000 potential claims may arise under contracts with language identical with that in . . . the contract in this case." The Comptroller General of the United States has interpreted a contract substantially identical with the one under consideration as denying reimbursement for Social Security taxes. 16 Comp. Gen. 790 (1937). Certiorari was granted in order to obtain a final determination of the question.

[6] Social Security Act, c. 531, 49 Stat. 620, Sec. 804, 210(b).

[7] Steward Mach. Co. v. Davis, 301 U. S. 548, 578.

and upon "the right to employ"[8] and as a payroll tax.[9] It is not—as taxes upon the privilege of selling, manufacturing or processing characteristically are—measured by the value of the privilege taxed, or by either quantity or price of what is manufactured, processed or sold. A tax on the processing or sale of an article, while an excise, commonly would be denoted a tax "on" the article processed or sold. The contract itself speaks of such taxes which may, in the future, be "paid by the contractor *on* the articles or supplies contracted for." (Ital. supp.) Thus, this contract was concerned with Federal taxes "on" the goods to be provided under it, whatever the occasion for the taxes. And a tax "on" the relationship of employer-employee—characterized as a tax on payrolls—is not of the type treated by the contract as a tax "on" the goods or articles sold.

The contract refers only to Federal taxes, existing or future, on "material", "articles" or "supplies." And additional compensation is provided to offset only Federal taxes of the type of sales taxes and processing taxes, "applicable directly upon production, manufacture, or sale" and actually paid on supplies delivered to the Government. Since a tax on payrolls, or on the relationship of employment, is not—but in fact is distinct from—the type of tax "on" articles represented by sales taxes and processing taxes, respondent is not entitled to the additional compensation which it seeks.

In view of our determination that the Federal Social Security tax was not contemplated by the contract, we need not discuss respondent's contention that the tax paid under the Maryland Unemployment Compensation Act was a tax "imposed . . . by . . . Congress."

The judgment of the Circuit Court of Appeals is reversed and that of the District Court is affirmed.

Mr. Justice BUTLER took no part in the consideration and decision of this case.

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[8] See, Carmichael v. So. Coal Co., 301 U. S. 495, 508.

[9] *Id.*, 506, 511.